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DEPARTMENT OF ACCOUNTING AND FINANCE

A Thesis On
Assessment of the Role of Audit Firms in Reducing Fraud

By
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STATEMENT OF CERTIFICATION

Addis Ababa University

School of Graduate Studies

This is to certify that the thesis assessment of the role of audit firms in reducing fraud in Ethiopia: prepared by Abdi Tadesse, entitled: An assessment of the role of Audit firms in reducing fraud : In Ethiopian private audit firms and submitted in partial fulfillment of the requirements for the degree of Degree of Master of Science (Accounting and Finance) complies with the regulations of the University and meets the accepted standards with respect to originality and quality.

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
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STATEMENT OF DECLARATION

I, Abdi Tadesse, declare that this study entitled "An assessment of the role of audit firms in reducing fraud in Ethiopia" is my own work. I have carried out independently the research work with the guidance and support of the research advisor.

This study has not been submitted to any degree/diploma in this or any other institution. It is done in partial requirement of the M.Sc Degree in Accounting and Finance.

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List of acronyms

AABE	Accounting and Auditing Board of Ethiopia
ACCA	Association of Chartered Certified Accountants
AF	Audit fees
AICPA	American institute of certified public accountant
ERCA	Ethiopian Revenue and Custom Authority
AABE	Accounting and Auditing Board of Ethiopia
ASA	Auditing standards authority
ASC	Audit Service Corporation
CPA	Certified public accountant
EFD	Eclectic Fraud Detection
GAAS	Generally accepted auditing standards
IA	Internal audit
IAASB	International auditing and assurance standards board
IAESB	International accounting education standards board
ICAA	Institute of certified accountants and auditors
IFAC	International federation of accountants
IIA	Institute of internal auditors
IPPF	International professional practices frame work
ISA	International standard of audit
NAF	Non-audit fees
NAS	Non audit service
OFAG	Office of federal auditor general
SEC	Security and exchange commission
SOX	Sarbanes Oxley Act
U.S.GAO	United states Government Accountability Office

ABSTRACT

This study examines the roles of external auditors in fraud reduction in Ethiopia including the factors that influence external auditors' responsibility and expert performance in detecting fraud. The study adopts questionnaire data and depth interviews research approach by combining data gathering instruments of research questions,

The questionnaire data were analyzed using descriptive statistics, and correlations, and data from interview were interpreted qualitatively. The findings of the study show that, auditors are responsible for detection and uncovering fraud, and are legally liable for subsequently discovered misstatement in audited financial statements

The results of the research result indicate that most of the private audit firms do not comply with professional ethics and lack independence from their client. This non-compliance came from self-interest, self-review and familiarity threats which results from having family, financial and personal relationship with their clients.

Unwillingness to look for fraud because of fear of spoiling good relationship with clients, too much trust placed on the auditees, management and employees, auditor not giving enough emphasis to audit quality, management not having fraud policy; and, failure to focus on high-risk fraud areas. Fraudsters collusion, Absence of clear interpretation of tax law /proclamation, absence of well-organized professional body in Ethiopia are listed among the most important challenges of auditors fail to detect fraud. The study also finds that the six variables which are, professional ethics, certification, practical experience, training, audit fee, and independence significantly influence the auditor's expert performance to fraud detection.

CHAPTER ONE

1. INTRODUCTION

1.1. Background of the Study

Theories on the demand for auditing provide a general framework for auditing, or at least for understanding it. Mautz and Sharaf (1961) define the purpose of theory in the following way: *“One reason, then, for a serious and substantial investigation into the possibility and nature of auditing theory is the hope that it will provide us with solutions or, at least, clues to solutions, of problems which we now find difficult”*.

For example, auditing theory helps explain why auditing is needed in the first place. What is the role or purpose the audit process is having in the communication between a company and its environment? Furthermore, auditing theory attempts to explain why some of the postulates and key concepts of auditing are so important (see Mautz and Sharaf 1961; Flint 1988).

Auditing theory also uncovers some of the laws that govern the audit process and its activities. Finally, it provides us with a framework for understanding the relationships and interrelationships between different parties of a firm. Financial reporting was earlier seen to be central to the monitoring purposes, but since the 1960’s the focus moved to needs and the provision of information to enable users to take economic decisions (Higson 2003).

Auditing is a process for the accumulation and evaluation of information whether a company’s financial statements are in compliance with established criteria and legislative requirement and confirm the information stated on the financial statement is materially correct and add value by forming an opinion which enhance the credibility of the information contained on the company’s financial statement (International Auditing and Assurance Standard Board, 2009).

From the above definition, the main role and responsibility of auditors is not only to satisfy the needs of individual client or employer rather to keep and act on the interest of the public which includes clients, creditors, governments, investors, the business and financial community, and others who rely on the objectivity and integrity of certified public accountants.

Therefore, the audit is valued by investors as a means of improving the quality of financial information. (Wallace 1980, 1987 and 2004) Auditing plays an important role in monitoring contracts and reducing the information risk (Watts et al. 1986b). Without an external audit the accounting information used for decision-making by several internal and external parties lacks credibility. Therefore the most important requirement of the external audit is to increase the credibility of financial statements generated from accounting information (Lee 1972). Principals contract auditors to view the accounting numbers, procedures used in compensation and bonus plans and any breaches of contracts (Watts et al. 1986a).

The increased credibility of the financial information potentially benefits both owners and management. Information asymmetry creates a need for an independent intermediary, the auditor, to verify and provide assurance of financial reports prepared by the management. Without the verification of the auditor managers would have an incentive to misrepresent the performance of the company and their management skills, since they could gain private benefits by such actions. (Eilifsen et al. 2006).

The American Accounting Association's (AAA) Committee on Basic Auditing, Concepts (1973) summarized the criteria that create the demand for auditing:

The potential or actual conflict of interest, Consequences of errors, Complexity and Remoteness. In Ethiopia several researchers like Mihret (2010), Abdella Mudesir (2009), Muluneh Beyene (2007), Adane Wudu (2014) ,have studied in different ways, however, this study attempts to fill the gap and proposes to ascertain the impact of auditor firms in reducing fraud ,providing the reliable financial statements, and identifying whether the organization uses the audited financial statement.

1.2. Statement of the problem

Most people do not realize what the responsibility of the auditor is according to SAS no1, codification of auditing standards and procedures :” the auditor has the responsibility to plan and perform the audit to obtain reasonable assurance about whether the financial statement are free of material misstatement, whether caused by error or fraud. Because of the nature of audit evidence and the characteristic of fraud, the auditor is able to obtain reasonable, but not

absolute, assurance that material misstatements are detected. The auditor has no responsibility to plan and perform the audit to obtain reasonable assurance that misstatement whether caused error or fraud, that are not material to the financial statement are detect”. In an attempt to stifle criticism and appropriately respond to the public’s demand for improved auditors’ performance, the American institute of certified accountant issued SAS no 82. The new auditing standard details the auditors’ responsibility to detect and report material misstatement in financial statement due to fraud. This is the first time the AICPA has used the word „fraud” rather than the more discreet word „irregularity”.

In developing countries like Ethiopia, the efficient practices of the auditors in their responsibilities have not yet developed very well (Muluneh 2007). Auditors only do their job in a way that secures their personal careers, their continuing contracts as auditors or promotes the other business interests of their firm rather than a way that fulfills their legal and moral professional obligation to shareholders and other stakeholders. Even when fraud appears in a business, they fail to express their opinion on the fraud committed and fail to detect financial statements where fraud committed lies. The Office of Federal Auditor General (OFAG) and the International Federation of Accountants (IFAC) through the International Ethics Standards Board for Accountants (IESBA) are the two known standard setting bodies at local and international level. However the application and proper implementation of these standards by the private audit firms deteriorated from time to time. (World Bank, 2007).

International Ethics Standards Board for Accountants (IESBA) develops, adopt and implement a high quality international ethics standards for accountants. As per section 100 Code of ethics of Professional accountants issued by IESBA and the directive issued by Office of Auditor General of Ethiopia during 2009, “A distinguishing mark of the accountancy profession is its acceptance of the responsibilities to act in the public interest and not to satisfy the needs of an individual client or employer”.(OFAG, Ethiopian Code of Ethics for professional Accountant ,2009).

Study made by World Bank “Reports on Observance of Standards and Codes (ROSC) “in 2007 indicates that due to broader duties and responsibilities, OFAG was not able to properly implement its duties granted under the above article. As a result, except issuing and renewal of audit and accountancy license, the role of OFAG on implementation and follow up of code of ethics of professional accountant and other ethics and audit practice related control in private

audit firms became limited and reduced from time to time (World Bank, 2007)

On the other side, the issue of noncompliance with code of professional ethics, lack of independence, issuing extremely very lower quality audit report, lack of respect for their profession, making unfair competition and promotion to get client between audit firms which is against OFAG, ACCA and other professional body code of professional ethics standard, lack of maintaining their responsibility to the public interest rather than satisfy their client interest and deteriorating the credibility and confidence of the public (both private and government stakeholders) on the audit report and other assurance service provided by private audit firms becomes the features of private audit firm. (ROSC ,2007).

The World Bank research and other study made by other researchers like Kaashun Golo and Deselagn Getie indicate that there is no any strong and organized accountancy and audit professional association to follow the work and activities of both audit and accountancy firms in Ethiopia. Even if there is some association like Ethiopian Professional Accounting and Auditing Association (EAPPP), Ethiopian External Auditor Association (EEAA) and Accounting society of Ethiopia (ASE) all of those professional associations are dormant, limited in capacity and not actively participating on the accounting and auditing profession.

Therefore, all the above discussed problems along with the gap in the literature need to conduct extensive research on the impact of audit firms in fraud detection.

1.3. Objective of the study

1.3.1. General Objective

The main purpose of this study is to assess the role of audit firms in reducing fraud Ethiopia.

1.3.2. Specific Objective

Based on the this objective, the following are the specific research answered by the study

- > To what extent do private external auditors exercise their professional role and responsibilities reducing fraud?
- > What constraints exist on private auditors in attempting to exercise their professional responsibilities?

- > To assess if ERCA uses the audited financial statement prepared by audit firms for taxation purpose.

1.4. Hypotheses Development

This hypothesis is based on the idea that characteristics of fraud reduction are based on the auditors' role.

To achieve the objective of this study, in addition to the specific objective presented above the following hypotheses concerning the auditor's expert performance to fraud reduction were analyzed.

H1: There is a significant positive relationship between auditor certification and auditors' fraud reduction capabilities.

H2: There is a significant positive relationship between training and auditors' fraud reduction capabilities.

H3: There is a significant positive relationship between practical experience and auditors' fraud reduction capabilities.

H4: There is a significant positive relationship between audit fee size and auditors' fraud reduction capabilities.

H5: There is a significant positive relationship between independence and auditors' fraud reduction capabilities.

H6: There is a significant positive relationship between professional ethics and auditors' fraud reduction capabilities.

1.5. Scope and Limitations of the study

This study is confined particularly, those audit firms working in Addis Ababa. The research focus on the assessment of audit firm's role in relation to fraud reduction in Ethiopia and assurance service to the business sector, government owned enterprise and other international and local nongovernmental organization.

However, most of the time, these private audit firm do not provide their service to government or civil service organization whose budgets come from central government treasury.

Lack of previous research studies and accessibility of sufficient current literatures on the subject

of auditor responsibility and fraud detection in the context of Ethiopian is another off-putting factor. The perception of other stakeholders in audit environment like the audit client, donors, banks, Ethiopian Commodity Exchange (ECE), Charities and civic society agency, creditors, national bank of Ethiopia and other stakeholders in the public are not considered under this research.

In this research ERCA was included but, could not be seen from audit client's viewpoint which is in fact relevant to include this to come up effective results and the researcher believed this will be another research area.

1.6. Significance of the study

This study is aimed at finding out the assessment of the role of external auditors in reducing fraud and enhancing the reliability of published financial statements.

The study has the following importance;

- > The study helps for the stakeholder of business environment to identify the level of responsibility of professional account and cross check whether they are discharging their responsibility as per the rules and regulation, the code of ethics for professional accountants and independence the threat, from the influence of their clients in order to produce a quality audit report that plays a significant role in reducing fraud in the country.
- > It will also give positive insight for audit firms on how to fight fraud in the country.
- > It enables figuring out the current status of audit firms in Ethiopia with the professions global picture.
- > Creating awareness in the minds of the public and the auditee's on the necessity of an audit.
- > This study will be of great importance to the government since it will help to determine the exact tax liability of the tax payers.
- > Contribution to the profession's development in Ethiopia.
- > Finally it can be used as a reference for further studies.

1.7. Structure of the study

The research deals with the role performed of audit firms in reducing fraud. The structure of this study is as follows. The first chapter presents the introduction part of the paper from this chapter;

the readers can gain a general understanding on the issues of fraud and the role of audit firms in reducing fraud related activities. Chapter two presents the literature review. It consists of the theoretical and empirical studies. Moreover, conclusion and knowledge gap related with the current study are included under this section. Chapter three deals with the research design and methodology and thus discusses how the research has been conducted. Under this chapter the rationality of each research approach was briefly discussed. In addition to this, the chapter also looks at the overall side of the population with its different features the sample size, methods of data collection and analysis techniques used under this research

Chapter four includes both data presentations and the analysis of the data collected. This chapter relates the research questions, applied methodologies and the finding of the research.

The final chapter, chapter five provides conclusion and recommendations based on the whole study of the research.

CHAPTER TWO

REVIEW OF RELATED LITERATURES

As stated on the above chapter the main objective of this research is to assess the role private audit firms engaged in Ethiopia and its overall effect on audit quality provided by them.

This chapter provide the readers an insight into different area of previous and existing literatures related to different variables like ,code of professional ethics and independence of professional accountant their experiences“ training audit fee size and the certification I with the objective of fraud reduction.

This chapter will help the readers in understanding the concepts related to this study, along with developing their knowledge regarding what opinions different researchers and authors hold regarding the topic of research.

The review has three sections. Section 2.1 presents a review of the theory of fraud and external auditors as a theoretical framework.2. This is followed by a review of the relevant empirical studies on fraud and auditors responsibility in fraud detection in section 2.2. At the last, conclusions on the literature review and knowledge gaps are presented in section 2.3.

2.1. Theoretical Framework

Preventing and detecting fraud can be improved through enhanced organizational status and professionalism. Since the internal auditors can directly monitor internal control adequacy and financial statement preparation, the Treadway Commission correctly characterizes their role as helping to provide the first line of defense against fraudulent financial reporting.

Thus, requiring all public companies to maintain an internal audit function should reduce the incidence of such fraud. The NCFRR's suggestion to have the chief internal auditor report directly both to a top officer not involved with the preparation of the financial statements and to the audit committee would help ensure that the internal audit group will be an effective monitor of the financial statement preparation process, free of coercion from potential perpetrators of fraudulent reporting. In addition to these reforms, professional certification of internal auditors should be required and increased emphasis should be placed on the development of auditing.

Because of this, this study tries to view some assumptions which is nearer to the concept of auditor responsibility and fraud detection to private audit firms. Hence, section 2.1.1 presents the concept of fraud. Then, section 2.1.2 presents theory of auditing .section 2.1.3, presents the factors influencing auditors" expert level of fraud detection capabilities. And section 2.1.4 presents the theories related auditors role and responsibility. Finally, section 2.1.5 the constraints that exist on auditors in their attempt to discharge responsibility.

2.1.1. Fraud

Fraud, according to (2004) and ICAN (2006), is an intentional act by one or more individuals among management, employees or third parties, which results in a misrepresentation of financial statements. Fraud can also be seen as the intentional misrepresentation, concealment, or omission of the truth for the purpose of deception or manipulation to the financial detriment of an individual or an organization which also includes embezzlement, theft or any attempt to steal or unlawfully obtain, misuse or harm the asset of the organization, (Adeduro, 1998 and, Bostley and Drover 1972). Fraud has increased considerably over the recent years and professionals believe this trend is likely to continue. According to Brink and Witt (1982), fraud is an ever present threat to the effective utilization of resources and it will always be an important concern of management. ISA 240 „The Auditor’s Responsibilities to Consider Fraud in an Audit of Financial Statement (Revised)“ refers to fraud as “an intentional act by one or more individuals among management, those charged with governance, employees or third parties, involving the use of deception to obtain an unjust or illegal advantage.

Aderibigbe and Dada (2007) define fraud as a deliberate deceit planned and executed with the intent to deprive another person of his property or rights directly or indirectly, regardless of whether the perpetrator benefits from his/her actions.

- Irregularity: is an intentional mistake or distortions of financial statement such as misrepresentation or misappropriation of assets.
- Misappropriation: is any dishonest or fraudulent act which includes such things as:

Unauthorized use, taking, or destruction of banks property for personal gain, or to purposely deprive the organization of its use,

Forgery or alteration of cheques, drafts, promissory notes, and securities,

Any taking or unauthorized use of bank's funds, securities, or any other assets,

Forgery or alteration of policy-related items, such as loans, assignments, changes in beneficiaries, etc.

The physiological theories of fraud explains that criminality is inborn and not radon. Clarke (1993) in what is known as the sociological theory of fraud explains that if it can be ascertained that certain groups or certain individuals are more likely than others to commit fraud, then they may be the likelihood to reduce the amount of frauds by removing the factors which predisposed these individuals towards perpetrating frauds. Cressey's fraud triangle theory describes a triangular relationship between opportunity, pressure, and rationalization (Cressey, 1971; Wells, 2001; Wilson, 2004).

Wilson (2004) describes "opportunity" as the ability to bypass or override controls meant to prevent manipulation, "pressure" the motivation to commit the fraudulent act, and "rationalization" as referring to the moral and ethical argument used to justify the act. What constitutes the key driver of frauds has been is an empirical question among scholars but research point that the same is not random.

According to Pollick, most people consider lying as fraud, but, in a legal sense, lying is only one small element of actual fraud. Fraud also involves complicated financial transactions conducted by the white financial reporting process and auditing functions.

2.1.2. Theories of auditing

There are several different theories that may explain the demand for audit services. Some of them are well known in research and some of them are more based on perceptions. Figure 1 illustrates four audit theories according to Hayes etal. (2005).

The policeman theory claims that the auditor is responsible for searching, discovering and preventing fraud. In the early 20th century this was certainly the case. However, more recently the main focus of auditors has been to provide reasonable assurance and verify the truth and fairness of the financial statements.

The detection of fraud is, however, still a hot topic in the debate on the auditor’s responsibilities, and typically after events where financial statement frauds have been revealed, the pressure increases on increasing the responsibilities of auditors in detecting fraud.

Figure1. Four theories of auditing (Hayes et al. 2005)



Source: Adapted from Hayes et al. 2005.

The lending credibility theory suggests that the primary function of the audit is to add credibility to the financial statements. In this view the service that the auditors are selling to the clients is *credibility*. Audited financial statements are seen to have elements that increase the financial statement users’ confidence in the figures presented by the management (in the financial statement). The users’ are perceived to gain benefits from the increased credibility, these

benefits are typically considered to be that the quality of investment decisions improve when they are based on reliable information.

The theory of inspired confidence (Theory of rational expectations) (Limperg1932) addresses both the demand and the supply for audit services. The demand for audit services is the direct consequence of the participation of third parties (interested parties of a company) in the company. These parties demand accountability from the management, in return for their investments in the company.

Accountability is realized through the issuance of periodic financial reports. However, since this information provided by the management may be biased, and outside parties have no direct means of monitoring, an audit is required to assure the reliability of this information. With regard to the supply of audit assurance, Limperg (1932) suggests that the auditor should always strive to meet the public expectations.

Agency theory (Watts and Zimmerman 1978, 1986a, 1986b) suggests that the auditor is appointed in the interests of both the third parties as well as the management. A company is viewed as a web of contracts. Several groups (suppliers, bankers, customers, employees etc.) make some kind of contribution to the company for a given price. The task of the management is to coordinate these groups and contracts and try to optimize them: low price for purchased supplies, high price for sold goods, low interest rates for loans, high share prices and low wages for employees. In these relationships, management is the *agent*, which tries to gain contributions from *principals* (bankers, shareholders, employees etc).

2.1.3. Factors influencing auditors' expert level of fraud reduction capabilities

In these section theories in respect to Factors influencing auditors' expert level of fraud detection capabilities has been reviewed.

2.1.3.1. Certification

Under proclamation no 332/2014 of the Accounting and Auditing Board of Ethiopia states that any person who satisfies the requirements relating to the qualifications in the field of accountancy and has a minimum of three years' practical experience in the field may apply to the board to be registered as certified public accountant in such form or manner as may be prescribed by the board.

Certification is the percentage of external auditors in the external audit function who have the CPA certification. The purpose of certification is to establish a reliable, standardizing testing instrument that adequately assess the levels of specialized competency necessary to practice proper financial statement examination (Rezaee and Burton 1992). Professional certification obtained from a formal education process demonstrates an individual auditor's minimal level of competency (Mui 2009).

2.1.3.2. Training

Among the factors noted to be influencing the auditor's capabilities to detect fraud, availability of continuous training of auditors is singled out as very cogent (Nystrom 1997). Auditors should have a complete foundation in audit training like computers and other information technology. They need to have the ability to realize the opportunities computers render to possible perpetrators of fraud as well as an ability to use computers in analysis and documentation of alleged fraud (Bologna et al.1993). an auditor to be effective as expert witness, he or she should have good communication skills, able to think logically while under pressure, and should have able trained to exhibit financial data in financial statements for improved fraud detection and deterrence through educational seminars and others means , including establishing qualification for the auditor, assisting parties who wish to retain the services of auditors, maintain the competency of auditor through continuing professional education (Nystrom 1997). Continuous learning can develop experience through methods such as case studies, and simulations to keep updated with fraud detection knowledge. Continuous learning in the fraud detection task is an important activity as it enables auditors to stay abreast of: (1) changes in the technical aspects of how fraud can be perpetrated; and (2) changes in the environment in which fraud can be perpetrated (Mui 2009).

2.1.3.3. Experience

Experience like the formal and informal training improves the capabilities of auditors to judge professionally (Gunasti, 2010). Experience along knowledge of auditors is an important factor in audit process Experienced auditors have comprehensive knowledge about the financial misstatements and deficiencies of accounting system of audited unit.

Lawrence [1999] finds that experienced auditors are somewhat reluctant skeptics while

inexperienced auditors are aggressive skeptics. Thus, audit experience could bias auditors away from predicting fraud for at least two reasons. First, auditors generally experience low rates of fraud occurrence during their careers. Even when auditors discover a material misstatement, that misstatement is usually due to unintentional error.

Second, auditors' incentives are structured such that there are disincentives to find fraud. Peecher et al. [2013] highlight that while auditors can be penalized for failing to find fraud, they are not rewarded for work to detect and prevent fraud. Nor are there any public regulatory rewards for performing audits of particularly high quality.

Since the auditors experience is an indicator of a high quality as it increases, in this paper it will be assessed whether a client company will switch to a more experienced one in order to promote the auditors quality of fraud identification.

Other strategies would suggest that the auditor should be composed of a particular and extensive experience which increases in accountability and reporting demands on fraud detection by the auditors themselves (Knapp 2000). Audit experience is related to how long the auditor works and to how many audit engagements have been finished (Suyono 2012)

According to Nystrom (1997), experienced auditor able to identify accounting problem areas, rank these problem areas or topics as necessary, and properly clarify the focal point of investigation or refocuses the investigation as new information is acquired and evaluated. The importance of experience can be demonstrated when the experienced auditor, having knowledge of many different types of fraud based on first hand examination experience, obtains a more effective plan of examination. The more fraud base the experienced auditor has been involved in, the broader his knowledge base (Bologna et al.1993)

Coklin (1993) found that someone with more experience in a specific field had more ability in developing specific cases related to his/her experience and Technically, the audit expertise will increase with more experience in doing audit tasks. More experience will give more audit quality, particularly in making audit judgments.

2.1.3.4. Audit Fees Size

Audit fees refer to the amount of fees received by auditors for their professional services based on such factors as the complexity of the services, the level of expertise, and many other factors. Sukrisno Agoes (2012) defines audit fee as "the amount of the charge depends, among others, the risk of the assignment, the complexity of the services provided, the level of expertise required to carry out the services of proficiency level, the cost structure of the firm concerned and other professional considerations.

The cost of external audits (audit fees) refers to the amount of compensation for services performed by external auditors.

The compensation for the services is related to the amount time used to complete the work and the value of services provided to the client or the firm. According to Al-Shammari et al.(in Fachriyah,2011), the cost of external audits can also be interpreted as a function of the amount of work done by auditors or the price per-hour and the level of service required.

Hoitash et al. (2007) found that when auditors negotiate with management regarding the tariff fees paid related to their works, it is likely that there will be a clear reciprocal concession which would reduce the quality of the audited statements. Elder (2011) states that audit fee reflect the fair value of the works performed by auditors and particularly their audits.

One aspect of professionalism that should be possessed by auditors is the ability to conduct audit works in accordance with auditing standards. This aspect, along with other professionalism aspects, determines audit fees for the work performed by auditors (Fachriyah, 2011). In carrying out their auditing duties, auditors should be guided by auditing standards that have been established by the Indonesian Institute of Accountants (IAPI), the common standards, standards of field work and reporting standards (IAPI, 2007). Common standards are a reflection of personal qualities that should be possessed by auditors. It is required that auditors have technical trainings and adequate expertise in performing audit procedures.

Auditing is the collection and evaluation of evidence about information to determine and report the degree of correspondence between the information and the criteria established. It should be done by people who are competent and independent (Arens, 2012). Auditing should be done based on the auditing standards established by the Indonesian Institute of Certified Public

Accountants (IAPI). Furthermore, auditors are required to have sufficient competence, so that they are able to carry out auditing processes in accordance with the established procedures. After conducting auditing processes, auditors will receive fees or remuneration from clients for their professional services. According to Lestari (2013) and Thalassinos and Liapis (2013) there are three determinants of audit fees: the client attribute, auditor attribute, and engagement attribute. Research conducted by Lestari (2013) has indicated that the three factors influence the dominance and non-dominance of audit fees. Obviously, the use of audit services is intended to prevent fraud and to control risks. Pramudji (2009) argues that the development in the field of audit services is in line with the change of paradigm, which will support the prevention of fraud and is able to control risks.

This study was conducted based on Lestari's (2013) research which examined the elements of audit fees based on such factors as client attribute, auditor attribute, and engagement attribute. Other variables were developed in the present study as the impact of the application of assessment factors, such as the correlation of audit fees to risk control and fraud prevention.

2.1.3.5. Independence

A professional accountant, member of assurance teams and firms should be independent in the performance of professional services for the client.

Independence requires the state of mind that permits the provision of an opinion without being affected by influences that compromise professional judgment, allowing an individual to act with integrity, and exercise objectivity and professional skepticism.

Independency on assurance Engagements: - the intended users of the financial statements require that auditor to be independent from the assurance client. The auditor must be both independent in mind and independent in appearance.

According to International Ethics Standards Board for Accountants (IESBA) section 290 and Ethiopian's code of professional accountant rule no 19 any professional accountant should be Independence from the audited entity and other outside interest groups. It is essential that auditors are independent and impartial, not only in fact or mind but also in appearance. (OFAG, Ethiopian Code of Ethics for professional Accountant , 2009)

> Independence of Mind

The state of mind permits the expression of a conclusion without being affected by influences that compromise professional judgment, thereby allowing an individual to act with integrity and exercise objectivity and professional skepticism.

> Independence in Appearance

The avoidance of facts and circumstances that are so significant that a reasonable and informed third party would be likely to conclude, weighing all the specific facts and circumstances, that a firm's, or a member of the audit team's, integrity, objectivity or professional skepticism has been compromised.

Besides, it requires that avoidance of facts and circumstances that are so significant that a reasonable and informed third party, including safeguards applied, would reasonably conclude a firm's or a member of the assurance team, integrity, objectivity or professional skepticism had been compromised.

An independent audit provides a necessary external check on the integrity of financial statements. Auditor's independence is important in the context of audit quality because the independent audit is critical to the credibility and integrity of financial statements. A lack of independence impairs an auditor's ability to exercise objective audit judgments and affects confidence in the audit process (Treasury 2010).

Alim (2007) found empirical evidence that auditor's independence had a significant effect on audit quality. Without audit service by an independent party, the reliability of financial statements could not be assured.

> Factors Affecting Auditors' Independence

As per IESBA, independence is potentially affected by self-interest, self-review, advocacy, familiarity and intimidation threats. As per PWC article titled Independence, at the heart of who we are expressed Independence is about objectivity, skepticism and integrity. It is the hallmark of the audit profession, at the heart of audit culture and fundamental to everything we do. Our mandate to audit public companies is founded on our independence and professional competence. Independence is so essential to public company audits, so there should be comprehensive and strict laws, regulations and professional standards to govern it. It is essential for both as firms and as individual's level. (PWC, 2012)

Audit independence refers to the ability of the external auditor to act with integrity and impartiality during his/her auditing functions. Public opinions about audit independence are based more on their perception of auditor independence than on actual independence. (Uchenna N, 2006).

> Review of regulation no 322/2014

Regulation No 322/2014 “Establishment and determination of the Accounting and Auditing Board of Ethiopia “was issued by ministry of council to announce the establishment of Accounting and Auditing Board of Ethiopia, as autonomous organ having its own legal personality. The Board is accountable to the Ministry of Finance.

As per Article 5 of the regulation the Board have the following objectives,

1. Promote high quality reporting of financial and related information by reporting entities,
2. Promote the highest professional standards among auditors and accountant.
3. Promote the quality of accounting and auditing service of the country.
4. Ensure that the accounting profession is used in the public interest.
5. Protect the professional independence of the accountant sand auditors

Article 6, Power and duties of the board, stated that in addition to the power and duties of the board specify on proclamation 847/2014 article 4.

The Accounting and Auditing Board of Ethiopia (AABE) has given around 16 additional power and duties includes under article 6 of regulation 322/2014.

From those power and duties stated under article 6 sub article 1 of the regulation 322/2014 AABE will establishment, publish and review of a Code of Professional Conduct and Ethics for certified public accountant and certified auditors which shall be consistent with code of ethics and professional code of conduct issued by International Ethical Standard Board of Accounts (IESBA)

Sub article 11 of article 6 state AABE establish requirement for continuing professional training programs and sub article 13 under this article also state the power and duties of AABE in implementing a sound quality assurance mechanisms to ensure high quality audit practices.

In addition to this, sub article 12 on the same article also state AABE have a power to take a

disciplinary action on certified auditor and accountants for any breach of the code of professional conduct and ethics issued by the board.

To conclude the overall idea of both the proclamation and the regulation, the AABE will implement and arrange all professional code of conduct and ethic and quality assurance mechanism on both accountancy and auditing sector. Those activities stated on the proclamation and regulation will totally change the current accounting and auditing environment of the country.

> Auditor Violation and Disciplinary Process

Rule No. 19 of the Ethiopian Code of Ethics for Professional Accountant's deals with the enforcement of the rule of conduct. As per the rule the Office of the Federal Auditor General is responsible for the enforcement of the ethical requirements described in this code of ethics and for taking appropriate disciplinary action until such time that a separate and competent body able to take on this responsibility is established by the government of Ethiopia.(OFAG, Ethiopian Code of Ethics for professional Accountant ,2009).

The following three points are the basis to take a Disciplinary action:

1. Failure to observe the required standard of professional care, skills or competence;
2. Non-compliance with Code of ethics; and
3. Discreditable or dishonorable conduct.

The disciplinary committee established by Federal Auditor General will ordinarily carry out the disciplinary proceedings. The proceedings should be held in a manner that is consistent with the legal requirements. This will ordinarily involve legal representation, taking evidence and keeping records of the proceedings. Based on such evidence the committee will made the following sanctions:

1. Reprimand;
2. Fine;
3. Payment of costs arisen from the disciplinary proceeding
4. Suspension of Certificate of Competence; and
5. Withdrawal of Certificate of Competence;
6. Warning,

7. The refund of the fee charged to the client,
8. Additional education and the work to be completed by another professional accountant at the expense of the disciplined incumbents

2.1.3.6. Professional code of ethics for accountants

The conceptual framework for the Code of Ethics states that principles and expectations governing behavior of individuals and organizations in the conduct of auditing. It describes the minimum requirements for conduct, and behavioral expectations rather than specific activities. Auditors' Code of Ethics is a system or code of behavior based on moral responsibility and obligation to explain how an auditor must behave. OFAG has empowered to regulate the accounting and auditing profession include licensing of all auditors in the country, issuing a Code of Ethics for Professional Accountants, and taking disciplinary measures on proven acts of misconduct by professional accountants.(Government of Ethiopia, Establishment of Office of Federal Auditor General, 1997)

In 2010, Proclamation 669/2010 was issued by House of Peoples' Representatives of the Federal Democratic Republic of Ethiopia; to amend the power, duties and responsibility of OFAG (The Government of Ethiopia, Federal Auditor General Establishment (Amendment) Proclamation 669/2010, 2010). Later at the end of December 2014, Financial Reporting Proclamation No 847/2014 was issued to shift the regulatory role of OFAG on accounting and auditing profession to the newly established board, Accounting and Auditing Board of Ethiopia(AABE) which was established by regulation no 322/2014(The Government of Ethiopia, Financial Reporting Proclamation No 847/2014, 2014).

Under proclamation no 332/2014 of article 4, the Accounting and Auditing Board of Ethiopia have the powers and duties to establish, publish and review a code of professional conduct and ethics for certified public accountants and certified auditors which shall be consistent with that of International Federation of Accountant or its successors.

The purpose of Code of Ethics is to promote an ethical culture in the profession of auditing and provides guidance to Auditors serving others (IESBA, 2013). Auditing is an independent, objective assurance and consulting activity designed to add value and improve an organization's

operations. It helps an organization accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control, and governance processes.(International Auditing and Assurance Standard Board, 2009)

As per the International Ethics Standards Board for Accountants (IESBA) standards issued on January 2011 and the code of ethics of professional accountant issued by the office of Federal Auditor general of Ethiopia, Any professional accountant should follow the fundamental principles of code of ethics of professional accountant though out his professional life (IESBA, 2013), (OFAG, Ethiopian Code of Ethics for professional Accountant, 2009)

The IESBA standard No 100.1 state that a distinguishing mark of the accountancy profession is its acceptance of the responsibility to act in the public interest. Therefore, a professional accountants „responsibility is not exclusively to satisfy the needs of an individual client or employer. When acting as the public interest a professional accountant should observe and comply with the code of ethics for its profession.

This code of ethics has three parts. Part A deals the fundamental principles of professional ethics for professional accountants. Part B illustrates how the conceptual framework is to be applied in specific situations. Part C applies to professional accountants in business.

2.1.3.7. Fundamental Principles for Code of Ethics for Professional Accountant.

As per International Ethics Standards Board for Accountants (IESBA), professional accountant is required to comply with the following fundamental principles:

2.1.3.7.1. Integrity

A professional accountant should be straight forward and honest in all professional and business relationship.

2.1.3.7.2. Objectivity

A professional accountant should not allow bias, conflict of interest or undue influence of others to override professional or business judgments.

2.1.3.7.3. Professional Competence and Due Care

A professional accountant has a continuing duty to maintain professional knowledge and skill at

the level required to ensure that a client or employer receives competent professional services based on current developments in practice, legislation and techniques.

2.1.3.7.4. Confidentiality

A professional accountant should respect the confidentiality of information acquired as a result of professional and business relationships and should not disclose any such information to third parties without proper and specific authority unless there is a legal or professional right or duty to disclose.

2.1.3.7.5. Professional Behavior

A professional accountant should comply with relevant laws and regulations and should avoid any action that discredits the profession. As stated above, IESBA part B and C of the code of ethics of professional accountant deal with the conceptual framework of the code ethics of professional. The next section will deals with how professional accountant can identify the treat and safeguards that can be faced during their audit engagement. (IESBA, 2013)

2.1.3.7.6. Threats for Fundamental Principles of Professional Ethics and Independence

Treats are broad range of circumstance, situation and relationship exist between the professional accountant and the clients that can be affect the fundamental principles of code of ethics of professional accountants. (IESBA, 2013)

When a professional accountant identifies threats to compliance with the fundamental principles, they should be evaluate of those threats and determines that, they are not at an acceptable level, and whether appropriate safeguards are available and can be applied to eliminate the threats or reduce them to an acceptable level. IESBA stated that any type of source of treat can be fall on any of the following categories

2.1.3.7.7. Self-Interest Threat

Where an auditor is financially dependent on the audit client or where an auditor or someone closely associated with him has a financial or other interest in the audit client. The auditor also depends on the management of the company to secure its re appointment as auditor (Importance of Auditor Independence, 2014).

2.1.3.7.8. Self-Review Threat

The threat that a professional accountant will not appropriately evaluate the results of a previous judgment made or service performed by the professional accountant, or by another individual within the professional accountant's firm or employing organization, on which the accountant will rely when forming a judgment as part of providing a current service

2.1.3.7.9. Advocacy Threat

The threat states that a professional accountant will promote a client's or employer's position to the point that the professional accountant's objectivity is compromised.

2.1.3.7.10. Familiarity Threat

The threat that due to a long or close relationship with a client or employer, a professional accountant will be too sympathetic to their interests or too accepting of their work.

2.1.3.7.11. Intimidation Threat

The threat that a professional accountant will be deterred from acting objectively because of actual or perceived pressures, including attempts to exercise undue influence over the professional accountant.

2.1.3.8. Safeguards for Threat of Professional Ethics and Independence

IESBA define safeguards are actions or other measures that may eliminate threats or reduce them to an acceptable level. Safeguards of any potentials treat can be categories as Safeguards created by the profession, legislation or regulation which include Educational, training and experience requirements for entry into the profession, Continuing professional development requirements, Corporate governance regulations, Professional standards Professional or regulatory monitoring and disciplinary procedures. (IESBA, 2013)

IESBA identify the following possible engagement-specific safeguards that can be set at work environment includes:

- a) Having a professional accountant who was not involved with the non-assurance service review the non-assurance work performed or otherwise advise as necessary.
- b) Having a professional accountant who was not a member of the assurance team review

the assurance work performed or otherwise advise as necessary.

- c) Consulting an independent third party, such as a committee of independent directors, a professional regulatory body or another professional accountant.
- d) Discussing ethical issues with those charged with governance of the client.
- e) Disclosing to those charged with governance of the client the nature of services provided and extent of fees charged.
- f) Involving another firm to perform or re-perform part of the engagement.
- g) Rotating senior assurance team personnel.

2.1.3.9. Sources of Threats

Section B of the hand book of IESBA identify major source of threats for professional ethics and independence are discuss

1) Professional Appointment

- a) Client acceptance: An auditor should consider whether acceptance of a new client would create any threats to compliance with the fundamental principles. Where it is not possible to reduce the threats to an acceptable level, an auditor should not enter into the client relationship.
- b) Engagement acceptance after client has been accepted: Before accepting an engagement, the auditor should consider whether acceptance would create any threats to compliance with the fundamental principles.
- c) Changes in a professional appointment: An auditor who is to replace an existing auditor should determine whether there are any professional reasons for not accepting the engagement.

2) Conflicts of Interest: An auditor should be alert to any circumstances that could pose a conflict of interest. A threat to objectivity or confidentiality may also be created when a professional accountant in public practice performs services for clients whose interests are in conflict or the clients are in dispute with each other in relation to the matter or transaction in question.

3) Second Opinions: An auditor may be asked to give a second opinion on an entity that is not an existing client. There may be a threat to professional competence and due care in circumstances where the second opinion is not based on the same set of facts that were made

available to the existing accountant or is based on inadequate evidence.

- 4) Fees and Other Types of Remuneration: For professional accountant in public practice quoting whatever fee by itself is not unethical but the main issue relating to fees and remuneration if the quoted fee for the engagement is too low there may be a possibility of threat to professional competence and due care which resulted from enabling to perform the engagement as per the applicable technical and professional standard at that price. This is one of the main concerns of many private audit firms in Ethiopia and also affects the overall quality and process of the auditing for an engagement.
- 5) Marketing Professional Services When an auditor solicits new work through marketing; there may be potential self-interest threats that affect compliance with professional behavior.
- 6) Gifts and Hospitality: - an auditor, or an immediate or close family member, is offered gifts or hospitality from a client. If the value of these gifts or hospitality is insignificant. It may create self-interest or familiarity threat to objectivity and it also occur an intimidation threat to objectivity may from the possibility of such offers being made public.
- 7) Custody of Client Assets An auditor should not keep custody of client monies or any other assets unless permitted by law. Acceptance of client assets will result a self-interest threat for both professional behavior and objectivity.
- 8) Objectivity-All Services:- an auditor should consider whether there are interests in, or relationships with, a client or directors, officers or employees.

2.1.4. Role and Responsibilities of External Auditors in Reducing of Fraud

An auditor has the responsibility for the prevention, reduction and reporting of fraud. Illegal acts and errors are the most controversial issues in auditing, and have been the most frequently debated areas amongst auditors, politicians, media, regulators and the public (Mahdisalehi and Alimansoury ,2009).

The Audit firm provides a crucial role in providing reasonable assurance to the quality of financial information presented to stakeholders and other users of financial statements. As an independent, objective party, shareholders, creditors and other interested parties rely on the audit report to determine whether to rely on the information for decision making. The two primary characteristics that most stakeholders expect from the external auditor are competence and

independence. State licensure requirements address the technical competency aspects of the external auditor. The state of independence is more difficult to determine. The role of auditors has not been well defined from the inception (Alleyne and Howard, 2005). Porter (1997) reviews the historical development of the auditor's duty to detect and report fraud over the centuries and shows that there is an evaluation of auditing practices and shift in auditing paradigm through a number of stages.

Boynton et al (2005) claim that auditors are required to be more proactive in searching for fraud during the course of an audit. External auditor duties now include considering incentives and opportunities presented to potential fraudsters, as well as rationalizations that the fraudulent acts are justified. Auditors are also expected to inquire more closely into reasons behind such matters as, for example, errors in accounting estimates, unusual transactions that appear to lack business rationale, and a reluctance to correct immaterial errors discovered by the audit. (ISA 240)

A study by Jensen and Meckling (1976) shows how a role for auditors arises naturally from the existence of outside ownership, or equity, claims against a firm. As managers share of firm ownership declines, they have the incentive to boost their own total compensation, including all types of fringe benefits, at the expense of the other owners. Potential investors, recognizing that the owner managers have this incentive, reduce the price they are willing to pay for shares in the firm. But if the owner-managers can commit to limiting their perquisites, investors will be willing to pay more for shares, benefiting the owner manager's efforts to expand the firm. Subjecting the firm's financial records to an independent audit can enhance the credibility of such a commitment by the owner-managers.

Jensen and Meckling (1976) further shows that similar considerations apply to a firm funded by debt, or bonds. In this case, the owner-managers borrow money to run the business. Here, too, the managers' incentives differ from those of the individuals funding the firm. After managers have raised funds from debt holders, they can benefit by investing the money in high-risk activities. Debt holders recognize the managers and shareholders incentive to pursue high-risk activities, potentially at their expense, and therefore demand a higher rate of interest, or a risk premium, on the money lent to the firm. However, by committing in a debt covenant to policies that limit debt holders risk exposure, the managers and shareholders may be able to reduce the premium. An independent auditor can help the managers and shareholders demonstrate to debt holders that such risk-limiting policies are being followed.

Similar considerations apply to the role of debt covenants and auditing in addressing the underinvestment problem. Myers (1977) analyzes, in which the shareholders of a firm with outstanding debt can have the incentive to reject investment projects with a positive net value if the proceeds would accrue to debt holders. Smith and Warner (1979) describe various types of covenants to protect bondholders from managers and equity holder's incentives to act against their interests. Auditing can help verify the accounting criteria in such covenants and help ensure that the agreements are honored. If those investments pay off, the managers can repay the debt holders the promised amount and keep the remainder for themselves. If the investments perform poorly, they can simply default on the debt. In this case, shareholders are on the side of the managers, since they, too, could benefit from high-risk activities once the debt has been issued.

According to the above researches, several factors may affect audit detection of fraud and irregularities.

The auditor is placed in a position enabling him to suggest improvement in the clients accounting system and controls as well as to offer ideas for improving financial planning, tax planning and clerical efficiency (Burton and Porter 1971).

The auditors aim is to determine whether the report prepared by manager conforms to the contracts provisions. The auditors verification of the financial information adds credibility to the report and reduces information risks; potentially benefiting both the owner and the manager. While auditing is only one possible form of additional monitory, the extensive presence of auditing in such situation suggests that auditing is a cost effective monitory device (Glover and Prawtt, 2004).

2.1.5. Auditor's Professional Responsibilities

The U.S. Government Accountability Office U.S.GAO (2007) cited by Muluneh 2007, publicized through internet that preparation of financial reports is the responsibilities of the auditee entity not the auditor. Thus, Officials of the audited entity entrusted with handling public and private resources and auditors of government programs or entity fulfill essential roles and responsibilities in ensuring that public resources are used efficiently, economically, effectively, and legally. Audit organizations also have the important responsibility of ensuring that auditors can meet their responsibilities.

These unique roles involve using sound management practices and providing professional audits and attestation engagements (U.S GAO). As explained by the U.S Government Accountability Office, the following are the auditors' Responsibilities:

In discharging their professional responsibilities, auditors need to observe the principles of serving the public interest and maintaining the highest degree of integrity, objectivity, and independence. The public interest is defined as the collective well-being of the community of people and entities the auditors serve. These principles are fundamental to the responsibilities of auditors.

Auditors should act in a way that will serve the public interest, honor the public trust, and uphold their professionalism. A distinguishing mark of a profession is acceptance of its responsibility to the public. This responsibility is critical when auditing in the government environment. GAAS embody the concept of accountability, which is fundamental to serving the public interest.

Auditors need to make decisions that are consistent with the public interest in the program or activity under audit. In discharging their professional responsibilities, auditors may encounter conflicting pressures from management of the audited entity, various levels of government, and others who rely on the objectivity and independence of the auditors. In resolving those conflicts, auditors are responsible for acting with integrity, guided by the precept that when auditors fulfill their responsibilities to the public, these individuals and organizations interests are best served.

To maintain and broaden public confidence, auditors need to perform all professional responsibilities with the highest degree of integrity. Auditors need to be professional, objective, fact-based, nonpartisan, and non-ideological in their relationships with audited entities and users of the auditor's reports. Auditors should be honest and candid with the audited entity and users of the auditors work in the conduct of their work, within the constraints of the audited entity's confidentiality laws, rules, or policies. Auditors need to be prudent in the use of information acquired in the course of their duties. They should not use such information for any personal gain or in any manner that would be detrimental to the legitimate and ethical objectives of the audited entity.

Service and the public trust should not be subordinated to personal gain and advantage. Integrity can accommodate the inadvertent error and the honest difference of opinion; it cannot

accommodate deceit or subordination of principle. Integrity requires auditors to observe both the form and the spirit of technical and ethical standards; circumvention of those standards constitutes subordination of judgment. Integrity also requires auditors to observe the principles of objectivity and independence.

Auditors should be objective and free of conflicts of interest in discharging their professional responsibilities. Auditors are also responsible for being independent in fact and appearance when providing audit and attestation services. Objectivity is a state of mind that requires auditors to be impartial, intellectually honest, and free of conflicts of interest. Independence precludes relationships that may in fact or appearance impair auditor's objectivity in performing the audit or attestation engagement. The maintenance of objectivity and independence requires continuing assessment of relationships with the audited entities in the context of the auditor's responsibility to the public. In applying GAAS, auditors are responsible for using professional judgment when establishing scope and methodologies for their work, determining the tests and procedures to be performed, conducting the work, and reporting the results. Auditors need to maintain integrity and objectivity when doing their work to make decisions that are consistent with the broader public interest in the program or activity under review. When reporting on the results of their work, auditors are responsible for disclosing all material or significant facts known to them which, if not disclosed, could mislead knowledgeable users, misrepresent the results, or conceal improper or unlawful practices. Auditors are responsible for helping management and other report users understand the auditors' responsibilities under GAAS and other audit or attestation coverage required by law or regulation. To help managers and other report users understand an engagement's objectives, time frames, and data needs, auditors need to communicate information concerning planning, conduct, and reporting of the engagement to the parties involved during the planning stages of the audit or attestation engagement (U.S GAO 2007).

On the other hand, as per U.S Government Accountability Office audit organizations(auditors) have responsibility for ensuring that (1) independence and objectivity are maintained in all phases of the assignment, (2) professional judgment is used in planning and performing the work and in reporting the results, (3) the work is performed by personnel who are professionally competent and collectively have the necessary skills and knowledge, and (4) an independent peer

review is periodically performed resulting in an opinion issued as to whether an audit organizations system of quality control is designed and being complied with to provide reasonable assurance of conforming with professional standards. While management is responsible for addressing audit and attestation engagement findings and recommendations and tracking their status of resolution, audit organizations are responsible for establishing policies and procedures for follow-up to determine whether previous significant findings and recommendations are addressed and are considered in planning future engagements (U.S GAO 2007).

Also Anderson (1984) pointed out that, auditors professional responsibilities are governed by the rules of professional conduct whose enforcement is handled exclusively by the local standards. Most of these rules, however, refer to the accounting and Auditing standards of the profession, which in turn influenced by the recommendations in local standards. Among the auditing recommendations, the most fundamental are GAAS.

Meigs, et al (1991), explores in their study, GAAS are authoritative rules for measuring the quality of performance. Also as per Arens and Loebbecke (2012), the existence of GAAS is evidence that auditors are very concerned with the maintenance of a uniformly high quality of audit work by all independent public accountants. If every public accountant has adequate technical training and performs audits with skill, care, and professional judgment, the prestige of the profession will rise, and the public will attribute more and more significance to the auditors' opinion attached to financial statements (Arens and Loebbecke, 1991).

Moreover, Lynch (2004) discusses that the auditor has no responsibility for the prevention and detection of fraud and error. As a responsibility, auditors should design audit procedures to obtain reasonable assurance that those frauds and errors which are material and might impair the truth and fairness have not occurred, or that if they have occurred they have either been corrected or properly disclosed in the financial statements.

The auditor should have a responsibility to report to the management and those charged with governance of an enterprise when the audit has brought to light any irregularities or errors. When the matter is material he/ she should ensure the management are informed promptly and that, where appropriate, a report is made to the board of directors or the audit committee. Auditors should report to the users of the audit report to the extent that in their opinion, the "true

and fair view” or “fair presentation”, is affected (Lynch, 2004).

Therefore, from the above researchers’ discussion it is wise to summarize that management of an entity is responsible for the efficient, economic and effective utilization of entity’s resources. Besides it is the responsibility of the management preparing financial statement for easy verification. On the other hand, it is the responsibility of auditors to form an independent opinion based on audit examination and to report the findings to the users of audited financial statements. Accordingly, auditor should base on standards or principles formulated by the professional and /or regulatory body to which they are members or by which they have been regulated.

2.1.6. Auditors Legal Responsibilities

According to Megs et al (1987), the auditors legal responsibility can be statutory, contractual or both. Statutory responsibility is based on the mandatory audit requirement in the federal and local business act. Contractual responsibility drives from an agreement mutually decided up on by the auditor and the client. Both may also agree to certain functions in addition to the statutory requirements; in such case, the auditor will be responsible to the client for both the statutory and the additional contractual requirements. Besides this, auditors must be familiar with the specific act applicable to each of their clients.

The auditor’s statutory responsibilities and company or national legislation consist of the general duty that auditors have to report to users on whether the financial statements of the company show a true and fair view or present fairly the financial position and results of its operations. Specific duties such as to consider whether the information in the management report is consistent with the financial statements and whether proper accounting records have been kept by the company were also considered as stippled in statutory requirements (Lynch, 2004).

As per Anderson (1984), legal responsibilities of the external auditor arise from one or more of statues, as interpreted by common law; contract, as governed by common low; and tort, as governed by common law.

From the above discussions, the researcher concludes that auditor is legally responsible for both contractual agreement made between the auditor and the client; and statutory audit requirements. From Ethiopian perspective auditing Standards are the criteria or yardstick against which the

qualities of audit results are evaluated. They provide minimum guidance for the auditor that helps to determine the extent of auditing steps and procedures that should be applied in the audit work.

Similarly, the Ethiopian Government Auditing Standards stated that the statement of auditing standards describes the basic principles which govern the auditors professional responsibilities and which must be complied with whenever an audit is carried out. It provides a framework within which professional judgment must be exercised and establish the minimum standard to be followed on individual audits (OFAG: Ethiopian Government Auditing Standards, 2004).

Due to absence of a well-organized and empowered professional accounting and auditing body in Ethiopia at the present time, there are no formalized professional standards issued by any authority in the country. However, OFAG have adopted minimum auditing standards incorporated in their respective audit standards which it has developed.

The task of preparing detailed ethical principles and rules is primarily that of the professional associations and that all members of the associations have the responsibilities to accept, implement and enforce such requirements. In Ethiopia, due to the absence of an organized strong national professional association there is no comprehensive set of ethical standards to govern the behaviors of professional accountants. In the case of authorized auditors, it is assumed that they adhere to the code of ethics set by the professional bodies to which they are members (OFAG, 2004).

2.1.7. The constraints that exist on auditors attempt to exercise their responsibility

According to Aamir, et al (2011), one of the foremost but uncommon problems for auditor would be an attempt of sophisticated fraud from the client's side, which is that a client purposefully wants to hide certain material misstatements so that the auditor could not detect it. The most common reason for the audit failure would be that an audit itself was not effective and efficient, or that the audit was not planned in a proper way. Due to the lack of proper planning, it is difficult for an auditor to assess the main and significant risks are present in the client firm, so in this way the auditor focuses on wrong aspects rather than the ones which need to be scrutinized. Weak knowledge of the auditor regarding the client firm is another factor, which could lead to an audit failure. This would be due to the fact that complete information or scenarios were not presented by the client to the auditor in a clear and adequate, and the opinion

presented by the auditor has been on the availability of provided information.

Aamir (2010) also justifies, an audit failure is not due to the process of audit involved in the audit engagement rather it is due to the unavailability of information. The consequences of an audit failure could be that an auditor is being sued due to the issuance of wrong audit opinion concerning the financial reports, or maybe you do not get paid for the audit services (with a smile).

But the authorities do look into the case and decide that who was guilty party in the audit failure and based on that the guilty party is subject to the charges in the law.

Further, According Aamir (2011) one of the reasons for audit failure is the time allocated for the audit engagement. For instance sometimes there are only 10-hours allocated out of which you have to both detect the problem and keep communication and coordination with colleagues. Due to budgetary concerns the time limit could not be extended and therefore it turns out to be difficult to discover problems and detect material errors within such short period of time. Other than this an audit failure could be due to improper audit planning, and due to mistakes in the planning process you can miss important factors in the audit of the client firm. And sometimes a risk is detected in the audit but then it is difficult to eliminate the risk because the time allocated to you do not allow you to do so. The consequence for the audit firm is that it would need to use the insurance in order to cover its mistakes within the audit. Other than this there is a governmental organization, which investigates the audit engagements of auditors and in reference to illegal or bad audit the license of the auditor could be cancelled as well. Aamir also added that apart from this the auditor loses his reputation as well, and the clients feel hesitant to work with such auditors, and in general would have its negative impacts on the brand name of the audit firm as well.

Audit firms reviews and evaluates client internal Controls and audits their financial statements in order to prevent material misstatements (MURYA 2010). Murya further noted that Auditors of higher quality are less willing to accept doubtful accounting methods and are more likely to report errors and irregularities revealed during the audit work.

2.1.8. Non-Audit Services Fees and Auditor Independence

The provision of audit fees (AF), non-audit fees (NAF) and auditor independence impacts on the

effectiveness which constrains the auditors.

The magnitude of NAF could impair auditor independence as NAS have the following drawbacks that threaten that independence. The first drawback is the self-interest threat. The auditor may become more reliant on the client when considering future revenues from non-audit services to that client (Becker et al. 1998). Thus, auditors may be willing to ignore clients' violations and breaches in order to protect their prospective revenues. Research on this issue showed diverse results. However, some previous Studies have documented that auditors are less likely to issue a going-concern modified audit opinion for clients that pay higher NAF (Sharma and Sidhu, 2001; Wines, 1994).

The second drawback is the intimidation threat, represented by the clients' ability to choose a different auditor in the future. This threat exists in a normal auditor-auditee relationship but it becomes stronger when the auditor can also lose fees from consulting services (Mayhew and Wilkins, 2003). Several studies DeAngelo (1981a); Antle (1984); Simunic (1984); Acemoglu and Gietzmann, (1997) have also argued that NAS may reduce independence if auditors expect future fees and there is a threat to replace them if audit reports are not positive.

A third major drawback of NAF is the self-review threat. Auditors are responsible for evaluating internal control and accounting systems. Thus, auditors are actually evaluating their own work, which can affect their independence. Auditors may be unwilling to criticize the work carried out by their consultancy colleagues, because doing so may lead to the audit firm losing lucrative consultancy services (Bartlett, 1991). Therefore, during the audit, auditors may jeopardize their independence by ignoring errors that may have resulted from advisory services provided by their own firm. A further drawback of providing NAS is the threat of familiarity. Rouckle (1995) argues that the trust established between auditor and client through NAS may lead to excessive trust that, in turn, leads to less testing of the clients accounting data.

On the other hand, NAS may provide some additional insights into the firm, which may increase audit efficiency. The audit findings are available to the advisory service, and knowledge spillovers can not only enhance efficiency but also the quality of both audit and consulting services (Peel and Donnell, 1995). Thus, the total quasi-rents from auditing and consulting services might be higher than the quasi-rents from auditing services. Therefore, the auditors independence can be increased if the auditor also provides NAS. Craswele[^] al. (2002) in USA

investigates whether fee dependence within the audit firms' offices jeopardizes auditor independence. They argue that if fee dependence affects auditors' independent judgment, then auditors are less likely to qualify the accounts. Fee dependence is examined at both national and local office levels in audit firms. They focus on audit fee dependence, and control for the effects of non-audit service fee dependence after the 1989 mergers. They measure the independent judgment in auditing by the tendency to issue qualified audit opinions. Their results show that the level of auditor fee dependence does not affect an auditor's tendency to issue qualified audit opinions.

However, Beeler and Hunton (2002) find that audit partners exhibited more biased decision-making in the presence of potential non-audit services, and this creates a perceived lack of auditor independence. They find evidence that the audit fee structure affects the partners' evaluation of evidence and their going-concern judgments.

Beck *et al.* (1988) hypothesizes that non-recurring NAS impair audit independence more than recurring NAS but finds no evidence that auditor independence is impaired significantly by NAS. Arrunada (1999a) finds that auditor independence is not impaired by the provision of NAS and, contrarily, it may enhance the auditor's independence if he has a diversified clientele. Similarly, DeFond *et al.* (2002) find no evidence that the level of non-audit fees affects auditor reporting decisions or their propensity to issue going-concern audit opinions. The previous author explains in another study, Arrunada (1999a), that an auditor with a large and diversified clientele is collectively dependent on all his clients but more independent of each individual client. He suggested that NAS increase the auditor specific assets, in another words, increase the auditor's size and reputation, which enhances the incentive for the auditor to keep high levels of audit quality as any failure to do so would create large potential losses.

Jenkins and Krawczyk (2002) test a wide range of non-audit services in the USA such as actuarial services, legal services and software training and find a positive relationship between accounting professionals and investors' perceptions of auditor's independence and objectivity and additional non-audit fees.

In the UK, Lennox (1999) examines the association between audit qualifications and NAS, The result shows a positive but insignificant relation between audit qualifications and NAS, which may support the theoretical argument of the possible impairment of the auditor independence by

NAS.

Four Australian studies used data from different periods to investigate the association between the incidence of a going-concern opinion decision and NAF. Barkess and Simnetts (1994) find that NAS fees are not related to the audit opinion decision. Craswell (1999) tests audit opinions and found that NAS fees are found to be not related to the audit opinion decision. On the other hand, the other two studies found that NAF affects auditor independence. Wines (1994) conclude that auditor independence is impaired for clients generating higher levels of NAF.

Sharma and Sidhu (2001) provide evidence of significant positive associations between NAF and the propensity of the auditor to issue a qualified going concern opinion. This result suggests potential independence threats. In New Zealand, Hay *et al.* (2006) examine the effect of NAF on auditor going concern opinion. Their results show no significant association between audit qualification or modification and NAF. This result is inconsistent with their expectation that New Zealand's small and limited growth market for audit and non-audit services would increase the client pressure on the auditor in order to preserve their client base and fee revenues.

The positive impact was also found in an empirical study in New Zealand by Gul (1989) who finds that bankers had higher confidence in auditors who conduct NAS, such as designing and installing financial and cost accounting systems.

The second stream of research has investigated the effect of the provision of NAS on auditor independence in appearance. These studies argue that, since auditor independence is hard to measure, even if independence is not really affected, independence in appearance is affected and the public may perceive that the auditors independence is impaired, which is more dangerous.

Audit firms have market pressures and incentives to maintain their integrity and objectivity because they may lose their client base if they lose their reputation. Thus, the economic consequences of reputation loss provide incentives to auditors to sustain and demonstrate a high level of independence. At least, auditors should appear independent to the capital market because independence of mind cannot be observed (Mautz and Sharaf 1961).

Solomon *et al.* (2005) examine the extent to which the perceived credibility of financial statements is a function of the public's perception of the auditor's independence, using an experimental case on ninety five participants. The results illustrate that participants have less

confidence in financial information audited by firms that at the same time provide significant NAS, suggesting that auditors are perceived to be less independent when they also provide NAS. In Europe, Quick and Warming-Rasmussen (2009) empirically investigate the impact of NAS on investors' perceptions of auditor independence in Germany, considering the recent number of changes to NAS regulations that have occurred in Germany, USA and other countries.

Their findings support the negative impact view, which is in line with most of the previous studies of auditor independence in appearance that were performed in Anglo-American countries, particularly the US. The effects of 19 different services were analyzed and they find that shareholders generally perceive a negative effect on auditor's independence if NAS are provided. Quick and Warming-Rasmussen (2005) investigate the impact of NAF on perceived auditor independence in Denmark. They find that shareholders, bank loan officers and journalists perceive a negative effect on auditor independence if NAS are provided. Their findings show that the type of NAS influences auditor independence.

Many other studies have documented the same negative association. Firth (1980) finds that there is a perception of auditor independence impairment when the amount of NAF is large in relation to AF. Beck *et al.* (1988) also states that the increasing bond between auditors and their clients, due to the provision of NAS, leads to a public perception of impaired auditor independence.

From the above illustrations, it can be observed that the vast majority of empirical studies of auditor independence in mind, as measured by issuing going concerns or qualified reports, failed to find evidence that NAF jeopardizes auditor independence, while the vast majority of studies of auditor independence in appearance find that NAF impair the auditor independence.

Francis (2006) reviews the NAS research literature over the past 40 years and concludes that even though there is no clear evidence linking the provision of NAS with audit failures, the literature finds that NAS can adversely affect the appearance of auditor independence, and this may be more than just a "mere perception" problem, because there is also evidence that stock prices are significantly lower for companies that pay their auditors large fees for NAS. Although academic research findings are mixed, many accounting regulators clearly believe that NAF has the potential to impair auditor independence. Following the financial scandals involving Enron,

WorldCom, Global Crossing and others, the SEC attributed these to audit failures due to the lack of auditor independence. Consequently, the SEC implemented new auditor independence criteria requiring the disclosure of audit and non-audit service fees and banned the provision of certain non-audit services that are considered as a threat to auditor independence.

2.2. Empirical Review

This section provides an overview of the previous research on external auditor role and responsibility to reduce fraud as well as external auditor's fraud detection expertise. There by focus on the relevant literature that relates to this research objective. Fraud is an inevitable cost of doing business. Organizations are responding to the pervasiveness of fraud by employing increased fraud risk management strategies (KPMG 2008). The factors examined by studies on the ability to detect the likelihood of fraud can be categorized into several dimensions: fraud risk indicators, auditor's roles, audit firm's roles, audit firm's characteristics, auditor's characteristics, auditor's ethical status, cognitive factors, personality, and audit task. Many researchers have attempted to examine the effect of forensic auditing on fraud detection, for example, Madumere and Onumah, (2013) examined the effect of forensic accounting on corporate fraud and performance outcome in the Nigerian manufacturing sector. Using a match sample of 306 manufacturing firms registered with the Manufacturing Association of Nigeria (MAN). Three hypotheses proposed and tested and the findings revealed that corporate fraud is on the increase in this sector of the economy, and the reason is that most managers want to be independent at the expense of their employers. That most managers incorporate firms that supply goods to their company at very high prices thereby increasing cost of production.

Aduwo, (2016) conceptually review the impact of forensic accounting toward utilizing professional judgments, accounting skills, auditing and law procedures to fight the dreaded disease of corporate liquidation and the paper concluded that forensic auditing can go a long way to influence financial scandals in corporate organization.

Eyisi and Ezuwore (2014) on their paper considered the roles of forensic auditors in combating fraudulent activities, distinction of forensic auditor and statutory auditor, characteristic of forensic auditor and impact of forensic auditor on corporate governance. The paper concludes that forensic auditors having improved management accountability, strengthened external

auditor's independence and assisting audit committee members in carrying out their oversight function by providing them assurance on internal audit report have impacted positively to corporate governance, thereby reducing corporate failure and impoverishment of investors.

Kosmas et al (2009) investigated the effectiveness of forensic auditing in detecting and preventing bank frauds in Harare, Zimbabwe. The study employed questionnaires, personal interview and documentary review to obtain information from respondents in thirteen commercial banks, four building societies, and four audit firms. The study revealed that forensic auditing department lacked material resources and technical know-how. As well that forensic auditing is confronted with interference from management and the profession has no clear recognition.

In the current empirical study, Modugu and Anyaduba (2013) examined forensic accounting and financial fraud in Nigeria. The study employed survey design in a sample size of 143 consisting of accountants, management staff, practicing auditors and stakeholders. The authors employed binomial test for data analysis and found that there is significance agreement amongst stakeholder on the effectiveness of forensic accounting in fraud control, financial reporting and internal control quality.

Okunbor and Obaretin (2010) examined the effectiveness of the application of forensic accounting services in Nigerian corporate organization in a sample of ten companies quoted in the Nigerian Stock Exchange by employing simple regression model for the test of hypothesis. The study revealed that the application of forensic accounting services by corporate organization in Nigeria is not effective in determine fraudulent activities.

Onuorah and Ebimobowei (2011) employed survey design to examine the effect of forensic accounting services in fraud detection in Nigeria banks by the use of Augmented Dickey- fuller, ordinary least square and Granger Causality test. The result revealed that the application of forensic accounting services affect the level of fraudulent activities of banks.

Adegbie and Fakile (2012) employed Chi-square and statistics package for social science to empirically evaluate forensic accounting as antidote to economic and financial crime in Nigeria. They tested four hypotheses. The study revealed that forensic accounting is a financial strategy to curb and resolve economic and financial crimes in Nigerian economy.

Okoye and Gbegi (2013) employed simple mean and standard deviation to investigate forensic accountants to planning management fraud risk detection procedures. They also used multivariate analysis of variance and analysis of variance ANOVA to compare their study with that of Asare and Wright (2004). The authors found that forensic accountants effectively modify the extent and nature of audit test when the risk of management fraud is high. They also found that forensic accountant should be involved in the risk of management fraud assessment process than consulting them.

Bressler (2011) studied the perception of attorney and judges in the court system as to what might enhance understanding of the role of forensic accountants in fraud investigation. The researcher employed conceptual analysis and found that forensic accountants must be well trained in the rules of evidence, financial data, accounting information system software and communication skills.

Enofe, Utomwen and Danjuma (2015) examine the role of forensic accounting in curbing financial crimes. The study adopts a survey research design. The population of the study comprises of staffs of selected banks. Primary data was used for the purpose of this research. This research work employed the use of structured questionnaire in eliciting the required data needed to test the formulated hypotheses. Regression analysis was utilized as the method of data analysis and the results will be used in testing the hypotheses specified in the study. The study reveals that there is need for forensic accountants in the Nigerian banking system; Forensic accounting is an effective tool for addressing financial crimes in the banking. Imoniana, Antunes and Formigoni (2013) aimed at analyzing the characteristics of forensic accounting services performed by accounting firms in Brazil, using an exploratory approach. Their findings conclude that the idea that frauds have been least detected by auditors begins to gain shape as auditors are more adequately trained to detect frauds instead of emphasizing the traditional segregation of duties and safeguard of assets.

Many researchers have attempted to examine the effect of forensic auditing on fraud detection, for example, Madumere and Onumah, (2013) revealed that corporate fraud is on the increase in this sector of the economy, and the reason is that most managers want to be independent at the expense of their employers. Aduwo, (2016) concluded that forensic auditing can go a long way

to influence financial scandals in corporate organization. Modugu and Anyaduba (2013) found that there is significance agreement amongst stakeholder on the effectiveness of forensic accounting in fraud control, financial reporting and internal control quality. Okunbor and Obaretin (2010) showed that the application of forensic accounting services by corporate organization in Nigeria is not effective in determine fraudulent activities. Onuorah and Ebimobowei (2011) revealed that the application of forensic accounting services affect the level of fraudulent activities of banks. Adegbe and Fakile (2012) revealed that forensic accounting is a financial strategy to curb and resolve economic and financial crimes in Nigerian economy. Okoye and Gbegi (2013) authors found that forensic accountants effectively modify the extent and nature of audit test when the risk of management fraud is high. Bressler (2011) found that forensic accountants must be well trained in the rules of evidence, financial data, accounting information system, and software and communication skills.

Enofe, Utomwen and Danjuma (2015) reveals that there is a need for forensic accountants in the Nigerian banking system, Forensic accounting is an effective tool for addressing financial crimes in the banking system and finally that Conventional accounting techniques are not effective in curbing financial crimes. Imoniana, Antunes and Formigoni (2013) conclude that the idea that frauds have been least detected by auditors begins to gain shape as auditors are more adequately trained to detect frauds instead of emphasizing the traditional segregation of duties and safeguard of assets. Most of these studies have explored forensic accounting to an extent but there is need to examine the extent of forensic auditor in combating fraudulent activities in order to impact on corporate governance of Nigerian corporate organizations.

The fraud risk indicators dimension includes factors such as quality of internal control (Matsumura and Tucker1992), and client integrity and competence (Bernardi 1994). (Moet 1997) treated the variable fraud risk indicators in aggregate by referring to them as high fraud risk or low fraud risk. In contrast,(Krambia- Kapardis 2002) provided subjects with a list of fraud indicators. Meanwhile, the auditor's roles dimension includes factors such as awareness of the high risk audit areas and evaluation of management integrity and competence (Krambia- Kapardis 2002). On the other hand, audit firm's role dimension includes providing incentives to probe fraud, ensuring that there is no pressure to complete the audit, and ensuring that

management has not restricted the scope of the work (Krambia-Kapardis 2002). Audit firm's characteristics dimension includes size (Moyes and Hasan, 1996; Owusu-Ansah, 2002), peer review, prior success in detecting fraud (Moyes and Hasan 1996), and practice review experience of auditor's firm (Owusu-Ansah 2002). Furthermore, auditor's characteristics dimension includes experience (Pincus 1984, Moyes and Hasan 1996), ability, motivation, prior probabilities about the existence of fraud (Pincus 1984), auditor's penalty and audit fee (Matsumura and Tucker 1997), CPA qualification, types of auditor (Moyes and Hasan 1996), and tenure of auditor (Owusu-Ansah et al. 2002). In addition, auditor's ethical status dimension includes moral development (Bernardi 1994). Cognitive factors dimension tests factors such as standard representations and multiple representations (Johnson et al 1995), and perceptual readiness (Moet 1997). Meanwhile, the personality dimensions includes category width (Pincus 1984), field dependence/independence (Pincus 1984; Bernardi 1994), locus of control (Bernardi 1994), and ambiguity tolerance/intolerance (Pincus 1984; Zimbelman and Waller 1999). Finally, the audit task dimension includes audit plan (Matsumura & Tucker 1992; Moyes and Hasan, 1996; Braun 2000), and risk assessment (Waller, 1993; Krambia-Kapardis 2002). Pincus(1984), Bernardi (1994), Moyes and Hasan (1996), Owusu-Ansah et al. (2002) and Carpenter et al.(2002) are in agreement that the auditors' experience is a significant factor that may affect the ability to detect the likelihood of fraud. Krambia-Kapardis (2002) develops a model called "Eclectic Fraud Detection" model (EFD) which aims to enhance the auditor's fraud detection ability. According to Krambia-Kapardis (2002), a basic premise of the EFD model is that fraud detection is preceded by a pattern-recognition/fraud risk-assessment decision-making process. In order to adopt the EFD model, rationalizations, opportunity and crime-prone personality (ROP) risk assessment model must be utilized. This fraud risk assessment model, however, is more or less resembled a prediction model when the subjects were actually required to indicate from the list provided, fraud risk indicators that were related to the fraud incidences that they had experienced. As a result this study may have recall and maturation problems because respondents are required to recall those fraud incidences that they had experienced. In addition, Arkes, et al. (1986); Boatsman and Moeckeland (1997); Sutton et al. (1994) have provided evidence that auditors are actually reluctant to use decision model in assessing fraud risk. Based on the discussion above, the present study notes that there need be a requirement for the auditor to actually perform the fraud risk assessment task. There need be to conduct research to

understand the potential factors influencing external auditors' ability to detect fraud. Consequently, the inability of the external auditor to detect the likelihood of fraud resolved. In the light of the studies discussed so far, this paper seeks to expand the literature by providing evidences on the fraud detection ability of the external auditors in Ethiopia. Particularly, this paper would be focusing on the audit firms' role in reducing fraud.

Moreover, this study addresses the pervasive risk of fraud by investigating external auditor's expert performance in fraud detection and their responsibilities. An earlier study by Mui (2009) identified the determinants of the individual auditor's fraud detection capabilities. These determinants were captured in the model of auditor expert performance in fraud detection. Mui (2010) developed new scales of measurement for each of these determinants. This current study employed likert scale measurement unlike Mui model is OLS as their independent variable uses continuous measurement. In the literature, fraud detection was considered to be an unstructured task with an impoverished learning environment (Libby and Luft 1993; Libby and Tan 1994).

Libby and Tan (1994) assessed the relationship between experience, knowledge, and ability with expert performance in other audit tasks. In their assessment of these relationships in the context of unstructured audit tasks with impoverished learning environments (i.e. ratio analysis and earnings manipulation), Libby and Tan (1994) reported significant relationships between these determinants and expert performance. Their results supported Bonner and Lewis's (1990) proposition that knowledge and problem-solving ability were the major determinants of auditor expertise in these audit tasks. The Mui (2009) study extended the Bonner and Lewis (1990) and the Libby and Tan (1994) studies by applying the determinants of auditor expert performance to the fraud detection task. The determinants of auditor expert performance in fraud detection are theorized in the model of auditor expert performance in fraud reduction proposed by Mui (2009).this model comprises(1) the determinants of auditor expert performance in audit tasks other than fraud detection established in literature(Bedard and Chi 1993; Bonner and Lewis 1990; Libby and Luft 1993; Moyes and Anandarajan 2002; Moyes and Hasan 1996; Shanteau 1992; Shanteau, Weiss, Thomas, and Pounds 2002; Tan and Libby 1997); and (2) the determinants unique to the fraud detection task identifies in an interview study by(Mui 2009). Mui (2009) in the interview study established that the determinants of auditor expertise for audit tasks other than fraud reduction that were established in the above mentioned literature namely,

certification, continuous learning, practical experience, analytical reasoning, data analysis skills, communication skills are also applicable to the fraud detection task. Further, the fraud detection task requires the auditor to possess unique capabilities in addition to the determinants established in the literature namely, mentoring technical skills, and the ability to work within a team (Mui

2009) . In addition to these determinants that are inherent to the individual auditor, the Mui (2009) study also identified that the ethical or unethical atmosphere in the organization in which the auditor performs audit work impacts on the auditors" fraud reduction capabilities. These determinants can be categorized as knowledge, problem solving ability, interpersonal skills, and external factors. The knowledge category refers to strategies auditors can adopt to develop their knowledge of fraud and fraud detection. The determinants in the knowledge category comprise practical on the job experience, mentoring, certification, and continuous learning.

Abdolmohammadi et al.(2004) established that possessing current knowledge is the principal attribute of top industry audit specialist.in the context of fraud reduction, the question in relation to possessing current knowledge is how can the auditor learn about the fraud reduction.

Bonner and Lewis (1990) established that knowledge about audit tasks can be established through direct experience and indirect experience with the audit task in the context of auditor expertise. Technical knowledge of audit tasks can refer to learning processes, i.e. how the auditor learns about the audit task. The individual auditor can develop their technical knowledge of the fraud detection task directly through practical experience and mentoring and indirectly through certification and continuous learning. Standards such as IPPF attribute standard 1210 specify the extent of information technology skills that an internal auditor should possess. Specifically, this standard requires auditors to have sufficient knowledge of key information technology risks and controls and available technology-based audit techniques to perform their audit work. However, this standard does not require auditors to have the level of expertise of an information technology auditor. Further, practitioners have found that few individuals possess a combination of specialized information technology skills and auditing skills (Mui, 2009). Interpersonal skills - specifically, the ability to communicate and the ability to work within a team - are the third category of determinants in the model of auditor expert performance in fraud detection. Good communication skills foster openness in contrast to fraud fostering concealment

(Hooks et al 1994). IPPF practice advisory 1210 Proficiency requires auditors to be skilled in „dealing with people, understanding human relations, and maintaining satisfactory relationships with engagement clients". In addition, a complementary determinant is the ability to work within a team. Teamwork in the context of fraud detection is audit team brainstorming. Fraud in a financial statement requires external auditors to brainstorm about the possibilities of audit in every audit (AICPA, 2002). The ASA 240 the auditors' responsibility to consider fraud in an audit of financial report equivalent of the SAS no.99 audit team brainstorming session is the discussion among the engagement team about fraud risk (ASA 240 paragraph 30).audit team brainstorming for fraud risk assessment generates more quality ideas compared with those generated by individual auditors. Further, audit teams are able to eliminate poor quality ideas (Carpenter 2007) required to possess oral and written communication skills to communicate clearly and effectively.

2.2.1. Conclusions and Knowledge Gaps

Even though, the aforementioned, the empirical reviews try to point out their findings as per their study area, it doesn't necessarily mean that the findings of their country necessarily apply for another country, this is because each nation has its own culture, economic background, political environment and other considerations that need to be taken into account. When we see the studies conducted in Ethiopia, some research tries to see from the perspective of auditors' role and responsibility that lacks to touch the fraud detection and prevention ability aspect of auditors while others only from independence perspective. With that, the present study takes an attempt to assess the role of audit firms in reducing fraud risk from the perspective of professional ethics of the auditors.

CHAPTER THREE

RESEARCH METHODOLOGY

This chapter also used to address appropriate methods assessing the role of audit firms in reducing fraud with justifications of selected methods. The chapter is structured as; Research Approaches (section 3.1), Research Methods Adopted (section 3.2) and data analysis method (3.3)

3.1. Research Approaches

Research approaches are mechanisms of attaining research objectives. The approaches are adopted to achieve the best possible of the research objectives. Research approaches are also adopted based on the feasibility of the selected approaches. The common research approaches are quantitative, qualitative and mixed research approaches.

3.2. Research Method:

The study adopted mixed methods approach. Mixed method approach focuses on collecting, analyzing and mixing both quantitative and qualitative data

3.2.1. A Quantitative Approach

This method is one in which the investigatory primarily uses postpositive claims for developing knowledge from cause and effect thinking, reduction to specific variables and hypotheses and questions, use of measurement and observation, and the test of theories, employees strategies of inquiry such as experiments and surveys (creswell,2009). Quantitative research approach uses two strategy of inquiry known as survey and experimental design. Survey research provides a quantitative or numeric description of trends, attitudes, or opinions of a population by studying a sample of that population. Quantitative approach uses surveys of cross-sectional or longitudinal using self-administered semi structured questionnaires or structured interviews for data collection, with the intent of generalizing from a sample to a population (Babbie, 1990). The data are collected on an instrument that measures attitudes, and the information collected is analyzed using statistical procedures and hypothesis testing.

Experimental research seeks to determine if a specific treatment influences an outcome by

providing a specific treatment to one group and withholding it from another and determining how both groups scored on an outcome (Creswell, 2009).

An alternate qualitative approach is one in which the inquirer often makes knowledge claims based primarily on constructivist perspectives (i.e., the multiple meanings of individual experiences meanings socially and historically constructed, with an intent of developing a theory or pattern) or advocacy/participatory perspectives (Creswell, 2003).

3.2.2. Research Method: Qualitative Aspect

In addition to the quantitative approach the study used qualitative approach more specifically face to face interview with auditors of ERCA. It allows the investigator some degree of flexibility at the time of interviewing for the pursuit of unexpected line of inquiry which will arise at the study progresses. Questions in the interview checklist were constructed based on the review of literature. In the process of preparing, testing and using the instruments, the following procedures were followed. The questionnaires and the interview guides developed based on literature review relevant to the issue and the specific objectives, both tools would be judged for their validity using professionals in the area and in the final study, the questionnaires and interview administered by the researcher. Hence, based on the above discussions of the three research approaches and by considering the research problem and objective, in this study, researcher used mixed research approach; the rationale for combining both quantitative and qualitative data is to better understand a research problem by combining both numeric values from quantitative research and the detail of qualitative research and to neutralize limitations of applying any of a single approach.

3.2.2.1. Survey Design

The response help to assess the factors that could explain the auditors' fraud reduction capabilities and responsibilities, their level of exercising professional responsibilities and constraints exist in attempting to exercise their responsibility. The research evidence was gathered by using both close-ended and open-ended questionnaires. Mixed questionnaires have many merits; the most important of this advantage is its considerable flexibility (McNabb 2005). The questionnaires were structured based on those used by (Prawitt et al. 2009, and Mui. With regard to the close- ended questions, the respondents were asked to indicate their level of

agreement on a five point Likert scale with the following ratings. Strongly agree (SA; or 5), agree (A; or 4), neutral (N; or 3), disagree (D; or 2), and strongly disagree (SD; or 1)

On this scale a score of 5 or 4 indicates that the item is perceived to be essential while a score of 3 or 2 indicates that the item is perceived to be fairly important, but not essential, while a score of 1 indicates that the item could be disregarded for being unimportant. Similar scales have been used by Yanchi Mui (2010) and Prawitt et al. (2009) were found suitable. With respect to the open ended questionnaires the respondents were asked to provide open ended responses to the questions that require opinion and if they have opinions they feel the researcher would find useful.

3.2.2.2. Sample Selection

According to the Accounting and Auditing Board of Ethiopia as of 2017, the total numbers of private audit firms authorized were 93. With regard to the sample size, the research applied a simplified formula provided by Yamane (1967) as cited by Yilma Muluken to determine the minimum required sample size at 95% confidence level, e error of 5 percentage points.

$$n = N \frac{1}{1 + N(e)^2}$$

Where n is sample size, N is the total number of study population.

Where e is the error of 5 percentage points

Based on the above formula 75 audit firms were selected for the study.

According to Cohen et al. (2005), covering the entire companies in the study makes the study difficult. Hence, to select auditors the researcher used random sampling. In random sampling each individual in the population has an equal probability of being selected which is important for the external validity of the study (Creswell, 2009). Since the aim of the study is to make theoretical inferences from the results of the study that are suitable for further empirical investigation in any other context, this random sampling is the most appropriate method.

3.2. Data Analysis Methods

As explained in the preceding part, the research is designed to follow a mixed method. To this end, both qualitative and quantitative data were used. Data collected using questionnaire were analyzed through descriptive statistics like mean, percentage, median, frequency distribution and correlation analysis using Statistical Package for the Social Scientists (SPSS). It helps to

describe what the data look like, where their center (mean) is, how broadly they are spread in terms of one aspect to the other aspect of the same data (Leedy 1989). The SPSS is used to find out percentages, mean values, frequencies, and correlation analysis as main means for summarizing the data. Data collected from the interview were interpreted qualitatively.

3.3.1. Description of the study variables

As it is already mentioned above the dependent variable in this study is auditor's expert performance to fraud detection. Auditor's expert performance to fraud detection is measured with the scales developed using the five-point Likert Scale of "1-Strongly Disagree", "2-Disagree", "3-Neutral", "4-Agree" and "5-Strongly Agree". As per the hitherto existing literature, it is possible to measure these variables by primary data Questionnaire. This measure is expected to bring a reliable result after the collection of the data and its analysis.

The correlation analysis below reveals that there is a relationship between one dependent variable (auditor's expert performance to fraud detection) against six independent variables (certification, professional ethics, experience, training, audit fee, and independence) was used for the study.

CHAPTER FOUR

DATA ANALYSIS AND INTERPRETATIONS

The previous chapter discussed appropriate methodologies to assess the role of audit firms in reducing fraud. This chapter presents the result and analysis of the survey method and semi structured interview. The chapter is organized into four broad sections. Section 4.1 presents Survey result, section 4.2 presents Interview result, section 4.3 analysis, and section 4.4 presents the Conclusion.

To analyze the raw data collected from sample private audit firms, the researcher used SPSS 24 version which is specialized statistics program that can provide sufficient tools for analyzing the collected data and excel application of the SPSS outputs. Therefore, the quantitative data from the questionnaires was analyzed using simple descriptive statistics (mean, frequency and percentage) and presented in the form of graph and table. This enabled the researcher to make the analysis and to see the impact audit performed by them of private audit firms in reducing fraud.

4.1. Survey Results

This section presents the result and analyzes the data collected using self-administered questionnaire from sample of 75 audit firms in Ethiopia. The section will be categorized as 4.1.1 Respondents profile; 4.1.2 Survey result on audit firms.

4.1.1. Respondents' Profile

It is necessary to analyze the demographic profile of the respondents to validate reliability of data collected. Accordingly the respondents were asked to respond to their gender category, level of education and the position of the firms. The information processed by SPSS is summarized as follows.

Table 4.1- Sex of respondents

Sex of Respondents					
	Sex	Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Male	66	88.0	88.0	88.0
	Female	9	12.0	12.0	100.0
	Total	75	100.0	100.0	

Source: SPSS Results and Own Computation

As indicated in the above table the gender proportion of female respondents is 12% while the male respondents were 88%. Though the ratio of the respondents not proportional and varied both category of gender were participated in the survey. This enables the researcher that there was no bias in the survey instrument related to the gender of the respondents.

Table 4.2- Education Level of the Respondents

Educational Level Of Respondents						
		Frequency	Percent	Valid	Cumulative	
				Percent	Percent	
Valid	Master degree and above	5	6.7	6.7	6.7	
	BA degree	70	93.3	93.3	100.0	
	Total	75	100.0	100.0		

Educational level of respondents

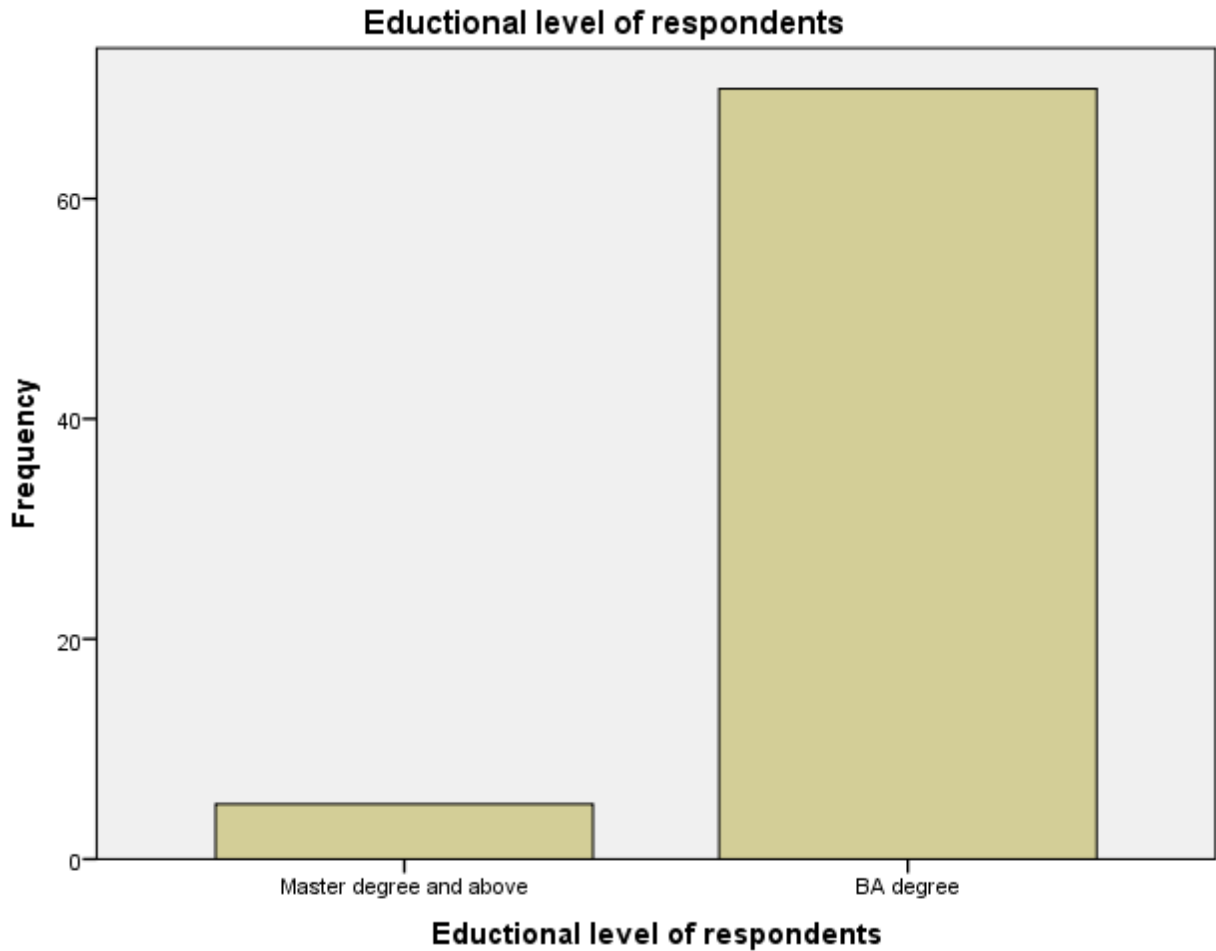


Figure 2- Educational level of respondents Source: SPSS Results

The level of education the auditors possesses contributes to effectiveness to fraud reduction. These increase academic competence of the auditors. The experience of the auditors reveals that a good education level has a positive impact on fraud reduction. As summarized in the above table, 93.3percent were qualified in degree and about 6.7 percent is above degree. This is an indication that the respondents are also at adequate education level to understand the concept of fraud reduction

4.1.2. Reliability Test of Instrument

One of the common methods to test the reliability and validity of data collected through questionnaire is use of Cronbach's alpha coefficient. Lee Cronbach (1951) defines Reliability as an attribute of an instrument used to measure consistency. Consistency indicates that an instrument has constructive value it used to measure. A commonly accepted rule of thumb for describing internal consistency using Cronbach's alpha is as follow.

Table 4.3- Cronbach's alpha

Cronbach's alpha	Internal consistency
$a > 0.9$	Excellent
$0.8 < a < 0.9$	Good
$0.7 < a < 0.8$	Acceptable
$0.6 < a < 0.7$	Questionable
$0.5 < a < 0.6$	Poor
$a < 0.5$	Unacceptable

Source: SPSS Results

The Cronbach's alpha for data collected for 6variables of audit firms, training, independence, professional ethics, audit fee size, certification and experiences is 0.749(approximated to 0.8).

Table 4.4- Reliability Statistics.

Reliability Statistics	
Cronbach's Alpha	No of Items
.749	6

Source: Survey Results

This indicates that the survey instrument used is highly valid and the data are highly consistent because the Cronbach's alpha is ranged in good measure of fraud reduction.

1. Training

Among the factors noted to be influencing the auditors' capabilities to detect fraud, availability of continuous training of auditors is singled out as very cogent (Nystrom 1997). Auditors should have a complete foundation in audit training like computers and other information technology.

Item	N	Min.	Max.	Mean	Std. Dev.
Do you think training on continue program development given for the auditors on how to collect data?	75	3	5	3.99	.688
Do you think a training given on the software application used in audit work?	75	1	5	3.73	.827
Is a case study and simulation given helps fraud detection knowledge for auditors?	75	2	5	3.87	.723
Do you think continuous program development help audit of fraud detection?	75	2	5	3.83	.760
Valid N (list wise)	75				

Source: SPSS result

As indicated in above table the mean value of the response computed based on Likert scale indicated the average agreement of respondents on the training.

Among the factors noted to be influencing the auditors' capabilities to detect fraud, availability of continuous training of auditors is singled out as very cogent (Nystrom 1997).

The overall mean of the training can be approximated to 3.85. Which indicate majority of the respondents agreed that training helps them during auditing their knowledge of fraud reduction.

The highest mean 3.99 indicates that majority of respondents agreed that the continuous program given for the auditor helps for the collection of source data (evidence). The result of the survey indicated by mean value of 3.87 shows that the respondent's agreed that a case studies and simulation given helps fraud detection knowledge for auditors. The result of the survey indicated by mean value of 3.83 shows that respondents agree you think continuous program development help audit of fraud detection.

The above table also indicated one area; the least mean 3.73 indicates that the respondents agreed that the application of software as an important for the auditors even if that majority of respondents agreed that the continuous program given for the auditor helps for the collection of source data (evidence) .This element also indicated the highest standard deviation (.827).

Finally, as it is indicated on the above table with a mean of 3.85, the respondents agreed that all the elements training mentioned above helps the auditors' knowledge in fraud reduction. According to the General Standards, the audit is to be performed by a person or persons having adequate technical training and proficiency as an auditor.

2. Professional ethics of auditors

Professional ethics of auditors is achieved when auditors adhere and follow to rules and regulations of auditing. Auditors' Code of Ethics is a system or code of behavior based on moral responsibility and obligation to explain how an auditor must behave. The survey result from the

respondents on Professional ethics of auditors is presented as follows.

Table 4.6- Professional

Item	No	Min	Max	Mea	Std.
1. Do you agree any professional accountant should follow the fundamental principles of code of ethics of professional accountant though out his professional life?	75	3	5	3.73	.644
2. Do to think that private audit firms that engage in Ethiopia properly follow and apply with all ethical standards issued by International Ethics Standards Board for Accountants (IESBA).	75	2	5	3.87	.811
3. Objectivity (Do the auditors are free from bias?)	75	3	5	4.04	.743
4. Integrity(DO the auditors are honest)	75	3	5	4.00	.678
5. Professional competence and due care	75	3	5	3.95	.676
6. Confidentiality	75	3	5	4.05	.715
7. Professional behavior	75	3	5	3.91	.619
8. Do auditor engaged in Ethiopia uses a system to identify the treat that affect their fundamental ethical behavior	75	3	5	3.88	.677
9. Do auditor has a capacity to evaluate the level of ethical threat they face during the auditing process	75	2	5	4.09	.681
10. Do you feel that it is the responsibility of the auditors to uncover fraud	75	1	5	3.95	.769
11. Do you think the auditors are liable for the losses of interested parties if failed to disclose potential fraud	75	2	5	4.03	.657
12. Do the auditors are liable if the company goes bankrupt due to fraud	75	3	5	3.96	.625
13. Valid N (listwise)	75				

Source: SPSS Result

The result of the survey indicated in the table above shows that the degree of agreement ranged from 1 to 5 by respondents in all criteria's of professional ethics of auditor. The Overall mean of the professional ethics of auditor for the twelve questions can be estimated to 3.96. The mean 3.73 on the above table show that the respondents agreed that any professional accountant should follow the fundamental principles of code of ethics of professional accountant though out his professional life. But there are rooms for improvement for this item of professional ethics of auditors as it shown by the lowest mean.

The highest standard deviation of the respondents and the mean 3.87 on the above table show that the respondents agreed that private audit firm that engage in Ethiopia properly follow and apply with all ethical standards issued by International Ethics Standards Board for Accountants (IESBA) .

The third item is indicated by the mean 4.04 show that the respondents agreed they are free from bias. The mean 4.00 on the above tables show that the respondents agreed they are honestly serving their clients. Again the mean 3.95 on the above tables show that the respondents agreed they apply Professional competence and due care during auditing activities.

The mean 4.05 on the above table show that the respondents agreed they were keep confidentiality which is one of professional ethics expected from all auditors.

The other fundamental principles of code of ethics of auditors indicated by the mean 3.91 on the above table show that the respondents agreed they apply Professional behavior while conducting auditing activities. The mean 3.88 indicated on the above table show that auditors agreed that auditor engaged in Ethiopia uses a system to identify the treat that affect their fundamental ethical behavior during conducting auditing activities. This item of professional ethics is indicated on the above table by 0.677.

1 The other item of professional ethics of auditors indicated by mean 4.09 on the above table that the respondents agreed show that auditor has a capacity to evaluate the level of ethical threat they face during the auditing process. As it was shown above the professional competence and due care have the mean 3.95, the respondent on the average agreed that it the responsibility of auditors to uncover fraud related activities. This is also indicated on the above table with the mean 3.95 with the minimum number 1 and maximum number 5.

The mean 4.03 indicated on the above table show that auditors agreed they are liable for the losses of interested parties if failed to disclose potential fraud.

The last element of professional ethics of auditors on the above table is indicated with the mean 3.96 auditors agreed that they are liable if the company goes bankrupt due to fraud.

As per IESBA section 210 and 220 this variables are potential source of threat for fundamental principles of objectivity and professional competence and due care.

From the above survey analysis the lowest mean among all items of professional ethics of auditors was shown is about any professional accountant should follow the fundamental principles of code of ethics of professional accountant though out his professional life.

3. Independence of the auditors

Independency on assurance Engagements: - the intended users of the financial statements require that auditor to be independent from the assurance client. The auditor must be both independent in mind and independent in appearance.

Table 4.7- Independence

Items	No	Min	Max	Mea	Std. D
Do you think auditors are free from advocacy threat (The threat that a professional accountant will promote a client's)	75	1	4	3.13	.600
Do you think auditors are free from self-interest threat(Auditors don't have financial interests with the audit client)	75	2	5	3.76	.732
Do auditors are free from Self-review threat (, on which the accountant will rely when forming a judgment as part of providing a current service.)	75	2	5	4.05	.733
Do auditors free from Familiarity threat(Auditors don't have family and personal relationship with client)	75	2	5	3.91	.825
Do you think auditors free from Intimidation threat (attempts to exercise undue influence over the professional accountant?)	75	1	5	3.09	.589
Do you think auditors don't accepts significant gifts from client	75	2	5	3.99	.668
Auditors disclose fraud only to the management and audit committee	75	3	5	3.84	.638
Valid N (list wise)	75				

Source: SPSS Result

The overall mean of the independence can be approximated to 3.88. This indicates that the respondents agreed the auditor independence in mind and appearance have an impact on fraud reduction. The highest mean 4.05 indicated on table above confirm that majority of respondents agreed that Self-review threat was the highest threat among the item of independence that have impact on fraud reduction capabilities of auditors. (Accountant will rely when forming a

judgment as part of providing a current service).

In addition to this, the mean 3.99 on the above table indicates the respondents also agreed that the auditors don't have to accept significant gifts from client which plays a big role for independence of auditor in reducing fraud related activities.

The mean of 3.91 indicates respondents agreed that Familiarity threat (family and personal relationship with client) have impact on the independence of auditors. The mean 3.84 on the above table indicates respondents agreed auditors disclose fraud only to the management and audit committee.

The respondents also agreed that self-interest threat having financial interests with the audit client have an impact on independence of audit firms. This item of independence was indicated by mean 3.76 on the above table.

The minimum mean 3.13 and 3.09 respectively in the above table indicates that respondents agreed that the advocacy threat and intimidation threat were not as such compared to other item of independence.

These items of independence were indicated by standard deviation of 0.600 and 0.589. The standard of United States General Accounting Office (amendment number 3, revised in 2002) states the following:

In all matters relating to the audit work, the audit organization and the individual auditors whether government or public should be free both in fact and appearance from personal, external, and organizational impairments to independence. Finally, the survey result on types of threats shows that self-interest, self-review and familiarity threats are the common type of threat that has been reflected on private audit firm industry.

4. Experience of the auditors

The importance of experience can be demonstrated when the experienced auditor, having

knowledge of many different types of fraud based on first hand examination experience, obtains a more effective plan of examination.

Items	No	Min	Max	Mean	Std. D
1. Do you think the direct technical knowledge of audit tasks enhance auditors fraud detection capability	75	3	5	3.97	.636
2. Do you think the number of years of auditing experience helps auditors on fraud detection ability?	75	2	5	3.99	.797
3. Do you think the repeated exposure to the fraud detection increase experience of auditors?	75	2	5	4.16	.698
4. Valid N (list-wise)	75				

Source: SPSS Result

The overall mean of the experience can be approximated to 4.02 .This indicates that on the average respondents agreed that experience helps auditor in fraud reduction. The highest mean (4.16) indicated on table above reveals that majority of respondents were agreed that repeated exposure to the fraud detection increases the experience of the auditors. The mean of 3.99 indicated on table above confirm that respondents agreed the number of years of auditing experience helps auditors on fraud detection ability which is very approached to the value of mean 4.

The more fraud base the experienced auditor has been involved in, the broader his knowledge base (Bologna et al.1993).

Respondents also agreed direct technical knowledge of audit tasks enhances auditors" fraud detection capability. This item of experience was indicated on the above table by mean of 3.97 and standard deviation of .636.

5. Audit Fees

In a competitive market for audit services it is reasonable to argue that when an auditor charges a premium fee to a client this will be associated with a better quality of assurance services

Table 4.9- Audit Fees size

provided.

Items	No	Min	Max	Mean	Std.
1. Do you think less audit fee reduce the scope of audit effort to detect fraud	75	3	5	4.03	.716
2. Do you think a large audit fee paid by the client doesn't make the auditor more economically dependent on the client?	75	2	5	3.97	.753
3. Valid N (list-wise)	75				

Source: SPSS

The overall mean of the audit fee size can be approximated to 4.0 .This means that the respondents agreed audit fee size have an impact on the scope of audit and makes the auditors economically dependent on client.

The highest mean (4.02) indicated on table above confirm that majority of respondents agreed that less audit fee reduce the scope of audit effort to reducing fraud.

According to Johnson (1998), examining the relationship between audit fees and auditors effort in detecting fraud is likely to provide a better insight into the market of audit services.

In addition, the mean 3.97 on the above table indicated that respondents also agreed that a large audit fee paid by the client doesn't make the auditor more economically dependent on the client even if the minimum number is 2.

6. Certification

Three questions were distributed for the respondents about certification.

Table 4.10- Certification

Items	No	Min	Max	Mean	Std. D
1. Professional certification obtained from a formal education process demonstrates an individual auditor's fraud detection competency	75	3	5	3.85	.672
2. Do you think certification establish a reliable, standardizing fraud testing instrument	75	3	5	4.05	.634
3. Is competency necessary to practice proper financial statement examination	75	3	5	4.07	.684
4. Valid N (listwise)	75				

Source; SPSS Result

The overall mean of the certification can be approximated to 4.0. The mean 3.85 showed that respondents agreed that Professional certification obtained from a formal education process demonstrates an individual auditor's fraud detection competency. The respondents were also agreed that certification establish a reliable, standardizing fraud testing instrument. This item of certification is indicated by the mean of 4.05. Of all item of the certification, the highest mean 4.07 indicated on the above table revealed that the respondents agreed that certification is necessary for proper financial statement preparation. This is indicated by standard deviation of

0.684. The purpose of certification is to establish a reliable, standardizing testing instrument that adequately assess the levels of specialized competency necessary to practice proper financial statement examination (Rezaee and burton 1992).

Finally, the respondents agreed that all items of certification stated above are important and helps the auditors in reducing fraud.

4.1.4. The extent of fraud reduction

In this section, the questionnaire results related to fraud reduction is presented. Two questionnaires were distributed to assess the existence of fraud in the company and the role of fraud reduction. The mean response of the two questionnaires under extent of fraud to users is 3.67. The respondents also agreed that it is the role of auditors reduces fraud. The mean of the respondents are 3.5 and the

standard deviation is 0.68.

The respondents agreed that fraud is the major concern of the company. The mean of the respondents are 3.85 and the standard deviation is 0.92.

Table 4.11- The extent of fraud reduction

Items	No	Min	Max	Mean	Std. D
1. Do you think fraud in company reduced by auditors?	75	3	5	3.85	.92
2. Do you think fraud major concern of the company?	75	2	5	3.5	0.68

Source; SPSS Result

As indicated on the table, 45.1% of the respondents agreed that fraud is a major concern for the company and 17.3% of the respondents strongly agreed. However, 37.6% have a neutral opinion, and none of the respondents strongly disagreed with this statement.

4.2. Constraints exist on external auditors in attempt to exercise their responsibility

Auditors are subject to different constraints when attempt to exercise their responsibilities. Table reveals descriptive statistics of constraints exist on external auditors in attempt to exercise their responsibility.

Table 4.12- Constraints exist on external auditors in attempt to exercise their responsibility

Items	No	Min	Max	Mean	Std. D
1. Do you think clients regularly don't demand for audit services?	75	3	5	4.03	.634
2. Do you think there is lack of cooperation from internal auditors?	75	2	5	3.91	.755
3. Do you think there is fear of losing client?	75	2	5	3.99	.797
4. Do you think clients demand unqualified opinion?	75	1	5	3.56	.687
5. Do you think there is poor record keeping of client's transaction?	75	2	5	3.76	.825

Source; SPSS Result

As it is indicated on the above table, the overall mean can be approximated to 3.96. The mean 4.03 showed that respondents agreed that clients regularly don't demand for audit services and this is the constraint on auditors while they are performing the roles and responsibility related to the audit services.

The respondents also agreed that they face lack of cooperation from internal auditors while they are performing the roles and responsibility related to the audit services. This is indicated by the mean 3.91 on the above table.

The respondents also agreed that fear of losing client is also another fear the faced while they are performing the roles and responsibility related to the audit services. This is indicated by the mean of 3.99 which is very close to 4. This is indicated by standard deviation of 0.797. The mean 3.56 respondents also agreed that clients demand unqualified opinion. This lowest mean compared to other item of constraint the auditors faced.

The respondents also agreed that poor record keeping of client's transaction also hinders them while they are performing the roles and responsibility. This is indicated by mean 3.76 on the above table.

Finally, from the above it is easy to understand that auditors faced different challenges from the clients while they are performing their duties.

4.3. Pearson Correlation Analysis

In statistics, the Pearson correlation analysis is a measure of the correlation (linear dependence) between two variables, giving a value between +1 and -1 inclusive. It is widely used in the sciences as a measure of the strength of linear dependence between two variables. The p-value, in Pearson Correlation analysis, attempts to provide a measure of the strength of results of a test, in contrast to a simple reject or do not reject decision.

In Pearson correlation analysis the value of strength of relationship (r) plays an important role in determining the level of relationships among variables. The significance level, $p < 0.05$ is also used to establish the relationship. This significance level shows that there is only 5 percent chance that the relationship does not exist, and 95 times out of 100 times the relationship among variables can be defined as having significant correlation.

The table below shows the results of the Pearson correlation analysis among the variables, testing of the hypotheses and interpretation of the Pearson correlation results would be presented in a separate section with the results of the regression analysis. Of the total of six explanatory variables tested in this study, there is a significant correlation between the variables (professional ethics of auditor, certification, training, experience, audit fee size, and independence) and the auditor expert performance to fraud reduction. The correlation between these six variables and auditor expert performance to fraud detection has positive value. Based on the results in table 4, there are positive relationships between auditor expert performance to fraud reduction and all of the independent variables, these shows that all of the hypotheses are supported.

Table 4.13- Fraud reduction and training correlation analysis result

		Fraud reduction	Training
Fraud reduction	Pearson Correlation	1	.054
	Sig. (2-tailed)		.644
	N	75	75
Training	Pearson Correlation	.054	1
	Sig. (2-tailed)	.644	
	N	75	75

Source: SPSS Correlation Result

Based on the results in table 4.13, there is a positive relationship between auditor expert performance to fraud reduction and training which is indicated by. 054. These show that the hypothesis is supported.

Table 4.14- Fraud reduction and Professional Ethics of auditors" correlation analysis result

		Fraud reduction	Professional Ethics of auditors
fraud reduction	Pearson Correlation	1	.002
	Sig. (2-tailed)		.986
	N	75	75
Professional Ethics of auditors	Pearson Correlation	.002	1
	Sig. (2-tailed)	.986	
	N	75	75

Source: SPSS Correlation Result

Again as shown in table 4.14 the auditors" performance to fraud reduction capacity and Professional Ethics of auditors has a positive relationship. This value is indicated in the above table (002.) These show that the hypothesis is supported.

Table 4.15- Fraud reduction and Independence of auditors" correlation analysis result

		Fraud reduction	Independence of auditors
fraud reduction	Pearson Correlation	1	.085
	Sig. (2-tailed)		.469
	N	75	75
Independence of auditors	Pearson Correlation	.085	1
	Sig. (2-tailed)	.469	
	N	75	75

Source: SPSS Correlation Result

As shown in the table 4.15, of the total of six explanatory variables (professional ethics of

auditor, certification, training, experience, audit fee size, and independence) tested in this study, there is a strong correlation between of Independence of auditors and the auditor expert performance to fraud reduction. This is indicated by .085 in the above table.

Table 4.16-- Fraud reduction and Experience of auditors" correlation analysis result

		Fraud reduction	Experience of auditors
fraud reduction	Pearson Correlation	1	.044
	Sig. (2-tailed)		.707
	N	75	75
Experience of auditors	Pearson Correlation	.044	1
	Sig. (2-tailed)	.707	
	N	75	75

Source: SPSS Correlation Result

From the above table 4.16, the auditors" performance to fraud reduction capacity and experience has a positive relationship. This value is indicated in the above table (044.) These show that the hypotheses are supported.

Table 4.17. Fraud reduction and Audit fee size correlation analysis result

		Fraud reduction	Audit fee size
fraud reduction	Pearson	1	.062
	Correlation		
	Sig. (2-tailed)		.596
	N	75	75
Audit fee size	Pearson	.062	1
	Correlation		
	Sig. (2-tailed)	.596	
	N	75	75

Source: SPSS Correlation Result

From the above table 4.17, the auditors' performance to fraud reduction capacity and audit fee size has a positive relationship. This value is indicated in the above table (.062) these show that the hypotheses are supported.

Table 4.18- Fraud reduction and Certification correlation analysis result

		Fraud reduction	Certification
fraud reduction	Pearson	1	.033
	Correlation		
	Sig. (2-tailed)		.780
	N	75	75
Certification	Pearson	.033	1
	Correlation		
	Sig. (2-tailed)	.780	
	N	75	75

Source: SPSS Correlation Result

From the above table 4.18, the auditors' performance to fraud reduction capacity and certification has a positive relationship even if their relationship is weak. This value is indicated in the above table (.033) and these show that the hypotheses are supported.

4.4. The roles and responsibilities of auditor in reducing fraud

Under this sub section, four questions were distributed to analysis the auditor's role, professional responsibilities and legal liabilities has been presented as follows.

Question1.is it the responsibility the auditors for the prevention, detection and reporting of fraud?

Table 4.19- The roles and responsibilities of auditor in reducing fraud

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	No	2	2.7	2.7	2.7
	Neutral	3	4.0	4.0	6.7
	Yes	70	93.3	93.3	100.0
	Total	75	100.0	100.0	

Source: SPSS result.

The survey result of respondents under table reveals that 93.3% most respondents agreed that it the responsibility of auditors to prevent detect and report fraud.

The survey result of respondents under table reveals that about 4% of the respondents remain neutral, while 2% of the respondents disagreed.

Question 2. Do private auditors are legally liable for subsequently discovery of misstated fraud

Table 4.20. Auditors' legal liability for subsequently discovery of misstated fraud

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Neutral	15	20.0	20.0	20.0
	Yes	60	80.0	80.0	100.0
	Total	75	100.0	100.0	

Source: SPSS result.

The survey result of respondents under table reveals that 80% most respondents agreed that auditors are legally liable for subsequently discovery of misstated fraud. The survey result also indicate that only 20% of the respondents was unable to give opinion (remain neutral) and none of the respondents disagreed. From this survey it can be said that majority of the respondents agreed that auditors are legally liable for subsequently discovery of misstated fraud.

Question 3. Do you think that auditor should assess management characteristics, if it may lead to fraudulent financial statement?

Table 4.21- auditors assess management characteristics, if it may lead to fraudulent financial statement.

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Neutral	6	8.0	8.0	8.0
	Yes	69	92.0	92.0	100.0
	Total	75	100.0	100.0	

Source: SPSS result.

The survey result of respondents under table reveals that 92% most respondents agreed that auditors should assess management characteristics, if it may lead to fraudulent financial statement. The survey also indicates that none of the respondents disagreed and only 8% of the respondents remain neutral.

Question 4: Do you consider that there should be an audit standard that would make auditors responsible for detecting and reporting fraud?

Table 4.22 - audit standard that would make auditors responsible for detecting and reporting fraud.

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Neutral	11	14.7	14.7	14.7
	Yes	64	85.3	85.3	100.0
	Total	75	100.0	100.0	

Source: SPSS result

The survey result of respondents under table reveals that 64% respondents agreed that auditors should consider audit standard that would make them responsible for detecting and reporting fraud during auditing. The survey also indicates that none of the respondents disagreed and only 14.7% of the respondents remain neutral.

4.5. Interview Results

An interview made with Auditors of ERCA and directors whether they use the financial statements prepared by audit firms (CPA).The major areas of questions were;

- > Do you use audited financial statements prepared by audit firms the for taxation purpose?
- > For which categories of the tax payers do you use?

The discussion from the interview is presented below.

In the first place the interviewees were asked whether ERCA is using the audited financial statement tax payers in the country. Accordingly the interviewees agreed that the use audited financial statement by certified public accountants (external auditors) and tax auditors check the tax payers“ liability that will be collected for the government.

The directorates also revealed that the office have been using audited financial statement for several years which simplify the work of ERCA tax auditors. An interview result with tax auditors also showed that they use audited financial statement for category tax payers of A and category B.

CHAPTER FIVE

CONCLUSIONS AND RECOMMENDATIONS

The aim of this chapter is to provide conclusion regarding the empirical findings and analysis of the research study. Finally, the study provides a recommendation on findings identified under this research.

5.1 Conclusions

This study set out to assess the role of audit firms in reducing fraud in Ethiopian private audit firms. Previous studies were reviewed and responses were analyzed and tested. Based on this, the study discovered that audit firms are an effective tool for addressing fraud in the clients' financial statement.

After all, the auditors irrespective of the challenges they faced in carrying out their professional duties, can detect and reduce fraudulent activities and legally held liable to uncover fraud.

Fraud detection was considered to be an unstructured audit task with an impoverished learning environment. Therefore, the continuous development program for developing external auditors' knowledge of the fraud detection task would have to be given for auditors which is unique to the fraud detection task.

Good ethical behavior of auditors increases the credibility and confidence of public on the assurance service provided by private audit firms. Unethical behavior also results in a lower audit quality which directly affects the credibility and confidence of public on the assurance service provided by private audit firms.

The results of the survey reveal that auditors followed the code of ethics or professional ethics of auditors which discusses the role and responsibility of auditors provided by regulatory and professional bodies in the implementation of code of ethics and the independence of auditors.

It was questioned whether the private audit firms are providing their professional service to the public by maintaining their independence and acts in compliance with the professional code of ethics. The researcher decided to assess the implementation of professional code of ethic and independence, identify those fundamental principles not complied by the audit industry, the

source and type of threats that affect the non-compliance of professional ethics, identify factors that affect and lead private audit firm not to be independent from their client, the effect of non-compliance of professional ethics against quality audit service provided by them, the role of regulatory and professional ethics on the current audit environment and at last the expectation of private audit firm on the new financial reporting proclamation.

The results of the survey reveal that auditors are responsible for detection and uncovering fraud. It has been identified through this study and in principle auditors are legally liable for subsequently discovered misstatement audited financial statements.

The main challenges auditors fail to detect fraud includes clients regularly don't demand for audit services, lack of cooperation from internal auditors, fear of losing client, clients demand unqualified opinion, and poor record keeping of client's transaction.

Absence of clear interpretation of tax law /proclamation, absence of well documented information on change implementation by tax authority, Lack of a professional accounting body which is strong and independent and absence of well-organized professional body in Ethiopia may cause auditors not be aware of and not to properly exercise their professional and legal responsibilities.

The auditors not to be able to perform with full objectivity and non-biasness, as too much trust placed on the auditees, management and employees, auditor not giving enough emphasis to audit quality, management not having fraud policy; and, failure to focus on high-risk fraud areas.

Finally, this empirical study has been conducted to critically examine the factors that could influence the auditor's expert performance to fraud detection. The survey results revealed that overall, external auditors had a positive perception of professional ethics certification, practical experience, training, audit fee, and independence. When the correlation analysis of auditor expert performance was applied to all external auditors, the value was positive coefficient .All variables have positive relation with fraud reduction.

Generally, the six determinants were analyzed by the correlation for the assessments of auditor expert performance in fraud reduction were considered to be good predictors of expert performance in fraud reduction.

5.2. Recommendations

The following possible recommendations can be forwarded in order to help auditors in to detect fraud, and in providing decision makers with relevant fraud reduction.

- > The independent auditor should be required to monitor the client's business environment for any red flags that warn Independent Auditors of potential fraud, and at least to consider performing relevant procedures designed to uncover such fraud. This requirement should enhance the likelihood of detecting fraudulent reporting. At the same time, it should also encourage courts to engage in a more deferential, procedural review of the independent auditor's performance, making it less likely that an auditor who complies with the requirement will be held liable for failing to uncover fraud.
- > Educational requirements should be stiffened to help ensure that the independent auditor has the analytical and ethical training to detect and prevent fraudulent reporting. Accounting programs at colleges and universities should be extended an additional year, and continuing professional educational programs should be designed to further develop the auditor's ability to uncover fraud.
- > All firms auditing SEC registrants should be required to join the SEC Practice Section. This would give the Professional Oversight Board sufficient leverage over auditing firms to make the peer review program a more effective weapon against fraudulent financial reporting.
- > Audit firms should perform their professional service based on International Standard of Auditing as stated on the Proclamation 847/2014 and implement International Standard on Quality control issued by IFAC for any service provided to the public.
- > Private audit firms should provide their professional services to the public in compliance with the rules and regulations stated by the regulatory bodies and being independent from any pressures made by third parties including the client.
- > The newly established board, Accounting and Auditing Board of Ethiopia, should prepare a well-organized code of professional conduct and ethics that strictly applied by all private audit firm in theirday to day operation. The Board should set effective and efficient follow up system to confirm the private audit firms are properly implementing and complying with

the code of professional conduct and ethical standards in their day to day professional service provided to the public. Moreover, there should be a serious, clear and reasonable disciplinary mechanism for those audit firms that don't comply with the code of professional conduct and ethical standards.

- > The audit firms and EPAAA in collaboration with the AABE should establish a strong, active power of voice professional associations or merge and reorganize all existing local professional association as a one and strong professional association.

- > The board, professional associations and the audit firms themselves at their level of responsibility should set a safeguard mechanism which is consistent with recommended safeguard mechanisms issued by international professional bodies like IESBA and ACCA.
- > The audit firms should stop unnecessary and unethical competition to get a new client and avoid the major source of threat reflected on the audit industry like low audit fee, client acceptance mechanisms, providing other assurance service unless proper safeguards system can be set and other sources of threat that deteriorate the independence and damaged the ethical standards and principles.
- > Auditors shall assign field auditors who are expert but if expert staff not exist they should train the existing staff in order to attain professional competence and also the staff should be aware of the development of their profession and senior auditor's should supervise field auditors.
- > Auditors should give an opinion based on the findings during an examination of financial statements not based on the wish of their client's.
- > Auditors need to "audit smarter" because they operate in a fixed fee environment, which limits the fees, that clients are willing to pay. This can be accomplished by the need for auditors to be more aware context in which the audit occurs and the fact that the nature and concentration of fraud varies by industry.
- > Auditors should exercise greater skepticism and rigorous assessment of management's integrity to identify the areas where fraud lies, which are also required by SAS No. 99. From an ethical viewpoint, external auditors should report any suspicion of fraud rather than remain silent.

- > There should be establishment of professional organizations in Ethiopia that would work on promoting the auditor's profession through well educating the auditor about his duties, responsibilities and restrictions on the engagement.

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Annexes

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Questionnaire

This project is entitled an assessment of the role of audit firms in reducing fraud in Ethiopian private audit firms. The investigator is Abdi Tadesse who is currently an MSc (in Accounting and Finance) student at Addis Ababa University.

The aim of this project is to examine the roles and responsibilities of external auditors in fraud detection in Ethiopia and also to investigate the factors that influence external auditors' responsibility and expert performance in detecting fraud. To supplement the data obtained from different sources, the investigator seeks to gather relevant information from a sample of 75 audit firms by means of self-administered question using semi structured questionnaire.

Participation in this project is completely voluntary, the questionnaire results will be recorded anonymously and strict confidentiality will be maintained. Individual responses will not be identified in the investigator"s MSc thesis.

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SECTION A: Background of respondents Please tick under appropriate option

1. Gender of the respondents

Female

2. Education levels

i. Masters degree and above

ii. BA degree

iii. Diploma and below

3. Your Position

Section II. Questionnaires

Please tick the following statements by indicating the level of agreement that you agree or disagree with the activities below:

Please kindly indicate the appropriate scale for your opinion by ticking (V) on the spaces that indicate your choice from the options that range from 5, strongly Disagree (SD), 4 Disagree (D), 3 Neutral 2(N), Agree (A) to 1 strongly Agree (SA)".

1	Training	Scale				
1	Is the training given for the auditors on how to collect data?	5()	4()	3()	2()	1()
2	Is there a training given on the software application used in audit work?	5()	4()	3()	2()	1()
3	Is there a case studies and simulation given for auditors on fraud detection knowledge?	5()	4()	3()	2()	1()
4	Do you think continuous learning influence audit of tax fraud detection?	5()	4()	3()	2()	1()

2. Professional ethics of auditor		Scales				
1	Do you agree that any professional accountant should follow the fundamental principles of code of ethics of professional accountant throughout his professional life	5()	4()	3()	2()	1()
2	Do you think that private audit firms that engage in Ethiopia properly follow and apply with all ethical standards issued by International Ethics Standards Board for Accountants (IESBA).	5()	4()	3()	2()	1()
2.1	Objectivity (Do auditors are free from bias?)	5()	4()	3()	2()	1()
2.2	Integrity (Do auditors are honest)	5()	4()	3()	2()	1()
2.3	Professional competence and due care	5()	4()	3()	2()	1()
2.4	Confidentiality	5()	4()	3()	2()	1()
2.5	Professional behavior	5()	4()	3()	2()	1()
3.	Do auditors engaged in Ethiopia use a system to identify the threats that affect their fundamental ethical behavior	5()	4()	3()	2()	1()
4.	Do auditors have a capacity to evaluate the level of ethical threats they face during the auditing process	5()	4()	3()	2()	1()
5.	Do you feel that it is the responsibility of auditors to cover fraud	5()	4()	3()	2()	1()
6.	Do you think auditors are liable for the losses of interested parties if they failed to disclose potential fraud	5()	4()	3()	2()	1()
7.	Do auditors are liable if the company goes bankrupt due to fraud	5()	4()	3()	2()	1()

3.Independence of auditors		Scales				
1.	Do you believe that auditor engaged in Ethiopia is independent in mind and in appearance?	5()	4()	3()	2()	1()
2	Auditors don't have financial interests with the audit client	5()	4()	3()	2()	1()
3	Auditors don't have business relationships with client	5()	4()	3()	2()	1()
4	Auditors don't have family and personal relationship with client	5()	4()	3()	2()	1()
5	Client don't involve and influence on preparation of financial statement by auditor	5()	4()	3()	2()	1()
6	Do auditors don't accepts significant gifts from client	5()	4()	3()	2()	1()
7	Auditors disclose fraud only to the management and audit committee	5()	4()	3()	2()	1()
4.Experience		Scales				
1	Do you think the direct technical knowledge of audit tasks enhance auditors fraud detection capability.	5()	4()	3()	2()	1()
2	Do you think the number of years of auditing experience have influence on fraud detection	5()	4()	3()	2()	1()
3	Repeated exposure to the fraud detection develop auditors fraud detection task	5()	4()	3()	2()	1()
5. Role and responsibilities of auditor in fraud detection		Scales				
1	Is it the auditor's responsibility include searching or detecting accounting fraud?	5()	4()	3()	2()	1()
2	Do Private auditors are legally liable for subsequently discovery of misstated audited financial statement?	5()	4()	3()	2()	1()
3.	Do you think that auditor should assess management characteristics, to determine if they may lead to fraudulent	5()	4()	3()	24()	1()
4.	Do you consider that there should be an audit standard that would make auditors responsible for detecting and reporting frauds?	5()	4()	3()	2()	1()
4.Audit fee size		Scales				
1	Do you think less audit fee reduce the scope of audit effort to detect fraud	5()	4()	3()	2()	1()
2	Do you think a large audit fee paid by the client doesn't make the auditor more economically dependent on the client?	5()	4()	3()	2()	1()
5.Certification		Scale				
1	Professional certification obtained from a formal education process demonstrates an individual auditor's fraud detection	5()	4()	3()	2()	1()

2	Do you think certification establish a reliable, standardizing fraud testing instrument	5()	4()	3()	2()	1()
3	Is competency necessary to practice proper financial statement examination	5()	4()	3()	2()	1()

7. Constraints exist on external auditors in attempt to exercise their responsibility.

1	Lack of clients regular demand for audit service	5()	4()	3()	2()	1()
2	Lack of cooperation from internal Auditors	5()	4()	3()	2()	1()
3	Clients demand unqualified opinion	5()	4()	3()	2()	1()
4	Fear of losing client	5()	4()	3()	2()	1()
5	Poor record keeping of client's transaction	5()	4()	3()	2()	1()

Section Two; Interview Guide

1. Do the ERCA use financial statement prepared by audit firms for taxation?

i. Yes

ii .No

If yes for what category of tax payers it is used elaborate-